OUR REF: FAIS 08491/12-13/ WC 1

20 February 2018

ATTENTION: Ms GERTRUIDA WYNETTA VENTER
Johnlyn Financial Advisory Services (PTY) Ltd
P.O. Box 7612
CENTURION
0046

Per email: johlynfs@mweb.co.za

Dear Mrs Venter,

Mr MICHAEL McNAMARA (complainant) v JOHNLYN FINANCIAL ADVISORY SERVICES (PTY) LTD (first respondent) and MS GERTRUIDA WYNETTA VENTER (second respondent): RECOMMENDATION IN TERMS OF SECTION 27 (5) (C) OF THE FAIS ACT, (ACT 37 OF 2002)

A. INTRODUCTION

1. During August 2010 complainant, Mr Michael McNamara, made an investment of R420 000 into The Villa Retail Park Holdings Limited [1](The Villa Ltd), a public property syndication promoted by Sharemax Investment (Pty) Ltd (Sharemax). The investment was made pursuant to the respondent's advice that Sharemax was a suitable investment. At the time, complainant was 48 and was preparing to retire. The objective of the investment was to provide income for his retirement.

2. Shortly after making the investment, complainant states that negative publicity about the problems in Sharemax began to intensify while respondent assured him that there was no problem with the company.

[1] Registration number 2008/017207/06

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3. Based on the complaints before this Office, Sharemax, at the time, was already struggling to meet investors' interest payments.

4. Neither the income nor the capital was ever repaid to complainant. He decided to file the present complaint against respondents for failing to advise him about the risks involved in Sharemax.

Delays in finalising this complaint

5. It is necessary to digress and explain the delays in finalizing this complaint in view of the Office's mandate to resolve complaints expeditiously. Sometime in September 2011, after the Office issued the *Barnes* determination[2], the respondent in that matter brought an urgent application to set it aside[3]. Before the fate of the application could be known, respondents sought an undertaking from this Office that it would not proceed in determining any other property syndication related complaints involving them.

6. Since no legal basis existed for respondent's demands, the Office continued to determine further property related complaints, to which respondents reacted with an urgent application for an interdict to stop the Office from filing the determinations in court, and issuing further determinations against them. The decision was finally delivered in July 2012 in favour of the Ombud. See in this regard *Deeb Risk v FAIS Ombud & Others*[4].

7. The Office continued to determine complaints involving property syndications after the High Court decision. However, in 2013, following the *Siegrist* and *Bekker* determinations[5] and the relevant appeal, a decision was taken by the Office to halt processing property syndication related complaints. The decision was not taken lightly, but was a precautionary and necessary risk management step, as the Office had, for the first time, sought to hold the directors of property syndication schemes liable for complainants' losses. The said appeal was finally decided in April 2015[6], after which the Office

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2 See E Barnes v D Risk Insurance Consultants FAIS-06793-10/11 GP 1

3 Respondent claimed that section 27 of the FAIS Act was unconstitutional

4 Gauteng High Court Division, case number 50027/2014

5 See in this regard FAIS-00039-11/12 and FAIS-06661-10/11.

6 See in this regard the decision of the Appeals Board date 10 April 2015.

resumed processing complaints involving property syndications with due regard to the decision. As many as 2000 complaints had to be shelved pending the Appeals Board decision.

B. THE PARTIES

8. Complainant is Mr Michael McNamara a male of adult age, whose details are on file with the Office.

9. First respondent is Johnlyn Financial Advisory Services (Pty) Ltd (reg number 2000/001296/07), a company duly incorporated in terms of South African law, with its principal address of business noted in the regulator's records as 83 Akkerboom Street Zwartskops, Ext 4, Centurion, Gauteng. The regulator's records confirm that the licence was issued in September 2005 and is still in force. First respondent is represented by its key individual Ms Getruida Wynetta Venter.

10. Second respondent is Johnny Venter an adult male Certified Financial Planner (CFP) whose details appear to be the same as those of first respondent. Second respondent is an authorised representative of the first respondent as provided for in the FAIS Act. At all times material hereto, second respondent rendered financial services to complainant.

11. I refer to the respondents collectively as "respondent". Where appropriate, I specify which respondent is being referred to.

C. THE COMPLAINT

12. During August 2010, at the age of 48, complainant, while preparing for retirement, had occasion to browse through Sharemax's website in an effort to find suitable investments for his security. He eventually sent through an enquiry to Sharemax in connection with their investments. Sharemax appears to have passed the lead to second respondent.

13. Second respondent, a veteran financial advisor with more than twenty-five years' experience in the financial services industry and boasting the qualification CFP, contacted complainant and went to meet him at his home.

14. During their discussion, complainant says he made a point of enquiring about the rumours regarding Sharemax at the time and was assured by second respondent that the rumours were unsubstantiated and of no concern. Complainant claims that second respondent never advised him of the risks inherent in the Sharemax investment.

15. On 23 August 2010, complainant invested in The Villa by making an electronic funds transfer into the trust account of Weavind and Weavind attorneys in the amount of R420 000[7]. However, he subsequently saw more articles in the newspaper about a problem with Sharemax.

16. He contacted second respondent who assured him that it was simply victimisation by SARS and the matter would soon be resolved. Complainant began to realise that there was no truth to second respondent's defence of Sharemax, with the result that their exchanges became heated. Complainant decided to file the present complaint against respondent for failing to advise him of the risks involved in the investment.

Relief sought

17. In his complaint, complainant asked for relief against respondents for the full amount of his capital of R420 000.

D. PROCEDURAL FAIRNESS

18. On 14 December 2015, a rule 6 (b) letter was sent to respondents inviting them to resolve the complaint with his client. No response was received.

19. On 30 January 2016, a further letter reminding respondent of the complaint was sent. There was still no response. On 1 November 2016 a notice in terms of section 27 (4) was sent to respondents, inviting them to provide their case against the complaint. The same notice was subsequently faxed to respondent. No response was received.

20. This recommendation therefore is made based only on complainant's version and his supporting documents.

[7] Proof of deposit supplied.

E. ANALYSIS AND RECOMMENDATION

The Villa Ltd Prospectus

Violations of Notice 459

21. From the onset, paragraphs 4.3 of The Villa Ltd prospectus made it plain that the directors of Sharemax, who also were directors of all the other Sharemax companies involved in the prospectus, were not going to comply with Notice 459.

22. In this regard, the prospectus made provision for disbursing investors' funds to pay for the entire shareholding of The Villa Retail Shopping Investments (Pty) Ltd (The Villa (Pty) Ltd), from Sharemax. There is no detail of the concomitant benefit for investors and neither is the full purchase price noted anywhere in the prospectus.

23. The prospectus disclosed (in paragraph 4.3) that investor funds will be lent to the developer, Capicol 1 via The Villa (Pty) Ltd, a subsidiary of the Sharemax group, well before registration of transfer of the immovable property into the name of the syndication vehicle.

24. The movement of the funds was illegal and a direct affront to Notice 459 (see Annexure A3, which contains a summary of section 2 (b) of the Notice) which is aimed at investor protection. The respondent, even in his answers to this office, says nothing about the infringement of the Notice.

Conflicting provisions of the prospectus

25. I refer also to the conflicting provisions of prospectus; in this regard paragraphs 19.10 and 4.3. First, paragraph 19.10 states that funds collected from investors would remain in the trust account in terms of section 78 2 (A) of the Attorneys Act. Investors' returns will be paid from the interest generated by the trust account. Paragraph 4.3 however, conveys that the funds would not stay long enough in the trust account, with 10% being released after the cooling off period of seven days to pay commissions. The same statement is made in the application forms that clients had to complete in applying for the investment. This payment too was in violation of the Notice.

26. There are two problems with the proposition that the investor's return was paid from the interest generated by the trust account. They are:

26.1 At the time, the interest payable by the bank on investments made in line with section 78 (2A) did not go beyond one digit. In fact, this office obtained information that the interest payable at the time was between 5.9% - 7%[8].

26.2 The prospectus is unequivocal that the funds would not stay long enough in the trust account to have accumulated any significant interest as they were withdrawn, firstly after ten days to fund commissions and subsequently, to fund the acquisition of the immovable property.

26.3 The prospectus states that the interest payable on the claim component of the unit will be determined from time to time by the directors[9].

Sale of Business Agreement (SBA)

27. The prospectus issued by The Villa refers to a Sale of Business Agreement (SBA) concluded between The Villa (Pty) Ltd and the developer, Capicol 1 (summary attached, annexure A4). Two types of payments are dealt with in the SBA. They are: payments to the developer, Capicol 1 (Capicol) and an agent, Brandberg.

Payments to Capicol

28. According to the agreement, investors' funds were moved from The Villa Ltd to The Villa (Pty) Ltd and advanced to the developer of the shopping mall. The payments were made well before transfer of the immovable property, and thus were in violation of the provisions of Notice 459. At the time of releasing the prospectus of The Villa, Sharemax had already advanced substantial amounts to the developer in line with this agreement (see paragraph 4.23 of The Villa prospectus). A brief analysis of the business agreement reveals:

28.1 No security existed for the loan in order to protect investors, which is clear from reading the prospectus and the agreement.

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8 http://www.fidfund.co.za/banking-options/credit-interest-rate-history/

9 See paragraph 9.3.1

28.2 The prospectus states that the asset was acquired as a going concern, even though the building was still in its early stages of development.

28.3 At the time the funds were advanced to the developer, the immovable property was still registered in the name of the developer. Although the prospectus mentioned the intention to register a mortgage loan, there is no evidence that it was registered.

28.4 The developer paid interest of 14%, from which Sharemax took 2% and paid the remaining 12% to the investors of the Villa.

28.5 The agreement is devoid of detail relating to the assessment of the developer's credit worthiness.

28.6 No detail is provided to demonstrate that the directors of the Villa had any concerns about the Notice 459 violations.

28.7 There are no details regarding the economic activity that generated the 14% return paid by the developer.

28.8 The conclusion is ineluctable that the interest paid to investors was from their own capital.

29. There was also no evidence that the developer had independent funds from which it was paying interest; besides which, if the developer had the financial standing to borrow such large sums of money at 14% per annum, it would have gone to mainstream commercial sources.

Payments to Brandberg

30. An entity known as Brandberg was paid commission in advance. The commission is said to have been calculated at 3% of the purchase price of R2 900 000 000 according to the SBA. There are no details of the benefit to investors for paying the amounts to this entity. No valid business case is made as to why commission had to be advanced in light of the risk to investors. There was also no security provided against this advance to protect the interests of the investors.

31. It is plain respondent's reply that the high risk involved in this investment was ignored or respondent simply had no resources to identify it.

F. FINDINGS

32. On the basis of the reasoning set out in this recommendation, the respondent failed in his duty to advise complainant about the risk in the investment, thus violating Section 7 (1). The section calls upon providers other than direct marketers to provide "*a reasonable and appropriate general explanation* of *the nature and material terms of the relevant contract* or transaction to a client, *and generally make full and frank disclosure* of any information *that would reasonably be expected to enable the client to make an informed decision*".

33. I add that the prospectus made it plain that the investment was far too risky, guaranteeing neither the capital nor the income.

34. Had respondent read and understood the prospectus, he would have never recommended the investment to the complainant. Respondent's conduct was negligent, which means he violated his duty to act with skill, care and diligence as provided for in section 2 of the Code.

35. Respondent has provided no documentation to demonstrate that, despite having had access to all the relevant and available information pertaining to complainant, the recommendation made was appropriate to his needs and circumstances.

36. As a consequence of the breach of the Code, the respondent committed a breach of his agreement with complainant in that he failed to provide suitable advice. The respondent must have known that complainant would rely on his advice as the expert in effecting the investment in Sharemax.

37. The representations made to the complainant were incorrect and in violation of section 3 (1) (a) (i) to (iv) of the Code. Complainant was simply not advised that the product was high risk and that he could lose his capital. There is no doubt that had the complainant been made aware of the risks involved in these investments, he would not have invested in the Villa Ltd scheme.

G. CAUSATION

38. The question that must be answered is whether respondents' advice caused complainants' loss. In the first instance, had respondent complied with the Code and sought investments that were in line with complainant's circumstances, there would have been no investment in Sharemax. In the event the complainant had still insisted on the investment, and assuming he had been made aware of the obvious dangers, respondent was obliged to comply with section 8 (4) (b) of the Code. It stands to reason that the respondents caused the complainant's loss, which loss must be seen as the type that naturally flows[10] from the respondents' breach of contract.

H. RECOMMENDATION

39. The FAIS Ombud recommends that respondents pay complainant's loss in the amount of R420 000.

40. The respondents are invited to revert to this Office within TEN (10) working days with their response to this recommendation. Failure to reply with cogent reasons will result in a final determination being made in terms of Section 28 (1) of the FAIS Act[11].

Yours sincerely

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NOLUNTU N BAM
OMBUD FOR FINANCIAL SERVICES PROVIDERS

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10 *Administrator, Natal v Edouard* 1990 (3)SA 581 (A); *Thoroughbred Breeders' Association of SA v Price Waterhouse* [2001] 4 All SA 161 (A), 2001 (4) SA 551 (SCA), paragraphs 46-49; Compare in this regard, *First National Bank v Duvenhage* [2006] SCA 47 (RSA).

11 "*The Ombud must in any case where a matter has not been settled or a recommendation referred to in section 27(5)(c) has not been accepted by all parties concerned, make a final determination, which may include-*
(a) the dismissal of the complaint; or
(b) the upholding of the complaint, wholly or partially…."