

IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

CASE NUMBER: FAIS 03950/14-15/ MP 5

In the case between:

MIKE LERATO MOGADIMA

Complainant

and

GO DIRECT STOCK MARKET INVESTMENTS (PTY) LTD

First Respondent

ACM GOLD AND FOREX TRADING (PTY) LTD

Second Respondent

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

A. INTRODUCTION

[1] Complainant invested R70 000 with first respondent. He believed he was purchasing shares in the second respondent. He was told that after the investment was made, he could “borrow” from the investment when needed. The investment was made in 2012 and when complainant tried to borrow some money, he was told that his policy is registered with a Mr. Kelvin Dube, who is one of second

respondent's brokers. A complaint was lodged at the offices of second respondent who referred complainant to this office.

B. THE PARTIES

[2] Complainant is an adult male artisan who resides in Mpumalanga. Complainant's full details are on file in this office.

[3] First respondent is Go Direct Stock Market Investments (Pty) Ltd, a private company registered according to the company laws of South Africa, having its registered address at Thornhill Office Park Midrand ("Go Direct"). A company search indicates that this company's principal business is "marketing" and the director is Cedric Mzoxolo Bezu (Bezu) who resides at F612 Castle Mansions 89 Eloff Street Johannesburg. Go Direct was initially registered as a close corporation which was subsequently converted to a private company. As a close corporation, the member's interest was owned: 50% by Bezu and 50% by Mbuso Abram Mthethwa whose address was given as 3600 Zirconium Lane, Clayville, Midrand.

[4] Second Respondent is ACM Gold and Forex Trading (Pty) Ltd ("ACM") a private company registered according to the Company Laws of South Africa having its principal place of business at 12th Floor Sandton City Office Towers. ACM is an authorised financial services provider with FSP number 26164.

C. THE COMPLAINT

- [5] Complainant's sister was employed by Go Direct as a sales agent. She told complainant that Go Direct can assist him in investing in overseas companies and that his returns will be paid to him in either US dollars or British pounds. Complainant then successfully applied for a personal loan from Capitec Bank in the amount of R120 000. He used R70 000 to invest in Go Direct and the balance was used to extend his father's home.
- [6] In November 2012, complainant met with Bezu who introduced himself as a director of Go Direct. They met in a coffee shop at the Eastgate Mall. Bezu came with a large stack of documents which complainant had to sign. Complainant points out that he noticed the ACM letterhead in the documents he signed. Bezu assured him that the money will be invested with ACM.
- [7] After signing the application forms, complainant proceeded to a branch of Capitec Bank where he transferred R70 000 into an account that Bezu provided. The funds were transferred from complainant's account into a Cheque account held by Go Direct. The transfer was done on the 18th November 2012. Proof of payment was provided to this office.
- [8] Complainant made the investment as he was promised "financial freedom" from the high interest he will receive. He was also informed that he could access the funds should he require.

[9] In 2013 complainant wanted to access his funds and approached ACM. It was then that he learned his money was not with ACM but with an individual called Kelvin Dube. He was told by ACM that his money was deposited “in the wrong account” and he was advised to contact this office. ACM refused to take any responsibility for complainant’s funds.

[10] After making the investment, complainant received a “Weekly Trading Statement”, dated 19th November 2012, the day after the transfer of funds to Go Direct. This statement shows a growth of 2.2% on the funds and is produced by Go Direct. The statement does not mention anything about ACM. I will deal with the significance of this below where I conclude that this statement is false. Complainant also received a set of “trading statements” from Go Direct; I considered these statements and there is nothing in them to show that this was complainant’s funds. The statements do not have complainant’s names and simply appear to be random printouts obtained from somewhere. Nor do the amounts in the statements bear any relevance to the amount invested by complainant. Again, these were false statements.

[11] Complainant has since not been able to contact Go Direct or any of its representatives or employees. He did not receive any of his promised returns and now wants his capital and interest paid back to him.

D. THE ISSUES

[12] The issues in this matter can be stated as follows:

- a) Whether or not Go Direct complied with the Act and Code when advising complainant to make the investment?
- b) Whether or not ACM breached the Act and Code in entering into a relationship with Go Direct?
- c) If the answer to the above two issues is positive, then what were the consequences?

E. COMPLAINANT PROFILE

[13] For purposes of this determination, complainants profile is relevant. This is the information we have on file:

- a) Complainant was 29 years old when he made the investment;
- b) Complainant obtained a level 3 welding certificate and was employed as a contract worker by Murry and Roberts at the Kusile Power Station.
- c) He earned between R14 000 and R15 000 per month, after tax, depending on how much overtime shifts were available.
- d) Complainant had no experience of investing and actually borrowed the money to invest in ACM and Go Direct. He is still paying off this loan.

The relevance of this profile is that there is no possibility that complainant was capable of carrying on any on-line trading in CFDs. This form of trading in forex is highly risky and there is the potential to lose more than 100% of ones investments. It is certainly not appropriate to trade with borrowed money, for a person of complainant's profile.

F. RESPONSE TO COMPLAINT

[14] The complaint as well as notices in terms of section 27 of the Act were emailed and posted to the respondents. This office received a response from ACM, which is dealt with below. However, no response was received from Go Direct. This came as no surprise as it became patently clear that Go Direct defrauded complainant of his money and no trading account was ever opened for complainant.

[15] I now set out ACM's response and why they say they should not be held liable for complainant's loss. Three written responses were received dated 18th September 2014, 18th April 2015 and 11th May 2015. The responses are summarised as follows:

- a) ACM is a technology company that provides a platform for individuals to invest in forex markets. The complainant was never a customer of ACM. There is no record of an account being opened in the name of complainant and ACM cannot say what Go Direct did with complainant's funds;
- b) When customers open an account they receive a trading account number which they use to deposit funds into ACM's bank account and use the number as a reference.
- c) Once money is deposited into the bank account ACM allocates it into the relevant trading account as per the reference number. ACM's only role is to assist customers with affording them the platform to execute trades or technical assistance. ACM does not trade for customers or inform them of which trades to take.

- d) Complainant, as a customer, never made a deposit into ACM's bank account.
Complainant made a deposit into Go Direct's bank account;
- e) Accordingly, ACM had no relationship with complainant and a relationship exists between Go Direct and complainant;
- f) Go Direct is an Introducing Broker to ACM. They are a separate company and none of Go Direct's employees work at ACM's offices. ACM refers to the "IB Agreement" entered into between Go Direct and themselves;
- g) On the 17th April 2015 a meeting was held with complainant and it was established that complainant's funds were paid into "the wrong account". The trading statements given to complainant by Go Direct were a fraud. There is no name on the statements; ACM issues trading accounts to all its clients in their names and all money collected from clients is deposited into a trust account in terms of the Act;
- h) As at 18th April 2015 ACM had no business dealings with Go Direct. After receiving a complaint from this office, ACM attempted to convene a meeting with Go Direct on the 14th April 2104. The latter did not show up and all attempts to contact them failed. After the complaint was received, Mr. Paulson of ACM contacted Go Direct and urged them to settle the matter with complainant. Again with no success. It was at that stage, in 2014, that all business with Go Direct was terminated;
- i) ACM explained that Go Direct were only mandated as a "sales agent" to direct potential clients to ACM representatives who then follow due process in terms of the Act. Accounts are opened for clients directly on ACM's system. If Go

Direct opened accounts on their system; then that was in contravention of the IB Agreement;

- j) ACM have no way of determining whether Go Direct deposited client funds into its trading account with ACM. Go Direct did have such an account but it was closed. When ACM started an internal investigation into Go Direct; the latter closed all its accounts and withdrew its balance on its trading account. At that point ACM terminated business with Go Direct;
- k) Finally, ACM expresses the view that Go Direct committed fraud.

GO DIRECT'S CONDUCT

- [16] It is undisputed that Go Direct provided financial advice and intermediary services, post it's IB Agreement with ACM. It is equally undisputed that when it marketed the product to complainant, it represented and held that it was an authorised representative of ACM and was licensed to give financial advice. Go Direct was not being truthful. This is a breach of the Code.
- [17] In giving advice to complainant, Go Direct made complainant believe that he was investing in shares. There was no such product; ACM mandated Go Direct to refer customers to it in order to open trading accounts to be traded by those customers. None of this was explained to complainant who would not have understood it in the first place. No information was given to complainant as to exactly what service and/or product was provided by ACM. Thus Go Direct breached the Act and Code by not providing information that was factually correct.

[18] It is clear that Go Direct and its directors committed common law fraud. The funds were obtained with no intention of making an investment on behalf of complainant.

[19] The money was not deposited in a trading account with ACM and Go Direct has never accounted for what they did with the funds. The only reasonable conclusion is that they appropriated the funds for themselves with no intention of returning any amount to complainant. All the representations regarding the investment were false and they were made with the sole intention of defrauding complainant of his funds.

This office recommends that Cedric Mzoxolo Bezu, Mbuso Abram Mthethwa and Kelvin Dube be reported to the South African Police Services; to be investigated for fraud.

[20] I find that Go Direct was in breach of section 7 of the Act and on the information before this office, they failed to comply with the following sections of the Code: 2, 3, 4, 5, 7 and 9.

ACM'S CONDUCT

[21] ACM expects to simply walk away from this matter on the basis that they had no relationship with complainant. They submit that there was a relationship only between complainant and Go Direct. However, ACM admit that they had a relationship with Go Direct; it is that relationship which must come under scrutiny. I will deal with this under various headings below.

LICENSING

[22] ACM is an authorised financial services provider. On ACM's own version they admit that when they entered into the IB Agreement with Go Direct, the latter was not licensed in terms of the Act. ACM submits that it was not necessary for Go Direct to be licensed as they were merely referring clients or customers to them. Go Direct was an independent broker. This is what ACM states:

"We have referral agreements in place with individuals and/or companies (we call them IB's) where they obtain customers under them who trade on our platform and we in turn have a revenue sharing agreement in place with the IB, whereby we pay them commission when these customers execute trades. (kind of like an external salesman who is not employed by ACM Gold)

Our IB referral agreement and arrangement does not require the individuals or companies to be licensed in order to do business with them and they do not trade on the customers behalf, they only find customers and introduce them to ACM Gold and the customers does the trading."

[23] There is absolutely no merit in this submission. It is not in dispute that Go Direct were giving financial advice and providing intermediary services as defined in the Act. The IB Agreement provides as follows in clause 4:

"For the duration of its appointment IB shall be obliged to facilitate the introduction of Products and or Services by Customers, exclusively from supplier in accordance with this agreement."

In clause 6 the following appears:

“IB shall be entitled to introduce the Products or Services at any retail or wholesale price as agreed to by Supplier in writing and supplier may determine any discounts, rebates or other terms and conditions relating to the sale of the products and or Services within the territory.”

ACM describes its services as follows:

“ACM Gold is a third party technology company that provides a platform for individuals to invest in the financial markets. We provide the deposit mechanism, pricing, liquidity and platform to enable these customers to trade in these markets.”

In clause 7 of the IB Agreement the following appears:

“IB undertakes that it will use its best endeavours to ensure that the Products and or Services are properly promoted and exploited by it in the Territory.”

[24] There can be no dispute that ACM were in the business of providing financial services and products as defined in the Act. It is this service which the IB, in this case GO Direct, was introducing or selling to members of the public. For Go Direct to do this, they had to be licensed in terms of the Act or they had to be appointed as a representative of ACM in terms of section 13 of the Act. It is a fact that Go Direct was marketing ACM’s products whilst unlicensed, nor were they appointed as ACM representatives.

The only conclusion to be drawn is that at all material times ACM and Go Direct were in contravention of Section 7 of the Act. GO Direct acted as broker for ACM without a license whilst ACM were conducting financial business with an entity that was unlicensed.

[25] ACM must have appreciated that it was doing business with an unlicensed company. They are an authorised FSP and were therefore familiar with the Act and General Code. They knew they were in breach of the law; they also knew that Go Direct was in breach of the law. Yet they continued to do business with Go Direct, regardless of the consequences.

[26] Significantly, the following appears in clause 15.3 of the IB Agreement under the heading “**RENDERING OF THE PRODUCTS BY IB**”:

“In carrying out its obligations under this Agreement, it shall comply with all relevant laws, including the FSB and the associated Regulations” (Emphasis added)

This contradicts ACM’s own version. They were obliged to check on Go Direct’s license compliance. They did not do so and even went ahead to sign an agreement knowing that Go Direct was unlicensed. ACM failed to comply with their own requirements.

DUE DILIGENCE

[27] As a licensed FSP, ACM was obliged to satisfy themselves that Go Direct and its directors were “fit and proper” to be appointed as brokers or representatives of the company. To this end ACM is expected to carry out basic due diligence to satisfy itself that Go Direct and the latter’s directors were credible, were persons of integrity and were trustworthy. This office called for ACM’s file and records and ACM provided no evidence that any due diligence was carried out. At the very least the following should have been done:

- a) ACM should have checked on Go Direct' s license to provide financial advice and intermediary services;
- b) ACM was obliged to satisfy themselves that Go Direct had the necessary skill, experience and capacity to give financial advice involving trading CFDs on the forex markets;
- c) ACM had to check whether GO Direct was financially credible and sound so as not to present a risk to customers. ACM had to consider Go Direct's trading history;
- d) ACM should have called for Go Direct' s financial statements and obtained a history from bankers and accountants;
- e) ACM had to do a similar due diligence on the directors and key employees of Go Direct to satisfy themselves that these are competent and trustworthy individuals who are fit and proper to market high risk investments.

There is no evidence that ACM carried out any of these very basic inquiries. It appears that ACM will do business with anyone who happened to walk in through their doors. ACM cannot now point fingers at Go Direct and call them frauds. Had they carried out basic due diligence, ACM would not have entered into an IB Agreement with Go Direct. This office has uncovered that Go Direct were not credible service providers and did not even have a permanent business address and no landline. The directors could not even be contactable on the mobile phones provided in their application form. ACM could have found this out had they made the most basic of inquiries.

[28] What ACM managed to achieve was to let loose on the unsuspecting public people who were not fit and proper to render financial services.

PUBLIC REPRESENTATIONS

[29] After entering into the IB Agreement, ACM provided Go direct with marketing materials and application forms bearing its name and logos. They also provided stocks of promotional and selling materials to Go Direct. This enabled Go Direct to represent to the public that they will be investing in ACM. In fact, the IB agreement, in clause 7.3 provides as follows:

“IB shall be entitled to attach to the Products and or Services, logo, label or other notices bearing IB’s name and address and indicating that IB is an authorised IB of Supplier.” (Emphasis added) “Supplier” is defined in the agreement as ACM.

In clause 7.7 of the agreement the following appears:

“IB shall be entitled, with the prior written consent of Supplier, to indicate at any place on its business premises, web site, user manuals and stationery, and in its advertising that it is an authorised IB of Supplier.”

The agreement even authorises Go Direct to use ACM’s Trade Mark.

It must then come as no surprise that at all material times, complainant believed he was investing in ACM. In fact, Complainant’s initial complaint was against ACM and not Go Direct. As far as he was concerned, his money was lost by ACM.

[30] Go Direct were given all the materials to effectively represent to members of the public that they were authorised by ACM to sell this product. Members of the public

justifiably so, accepted that they were investing in ACM and not in Go Direct. The fact that complainant deposited the money into a Go Direct account cannot assist ACM. On ACM's own version, they had no control over how Go Direct received funds from potential customers and how they dealt with such funds. It is a fact that ACM admits to having no effective oversight over the activities of Go Direct.

[31] ACM had no system to ensure that client funds with Go Direct were deposited in their account and not simply stolen. ACM could reasonably foresee that client funds may be deposited into the "wrong account" and took no steps to provide effective oversight and control over Go Direct. They could reasonably have foreseen that, absent proper oversight and controls, members of the public could suffer harm through loss of their investment. ACM were accordingly under a duty of care to ensure that their appointed IB complied with the Act and Code thereby minimizing the risk that Go Direct prey on unsuspecting investors. In breach of this duty ACM failed to take any reasonable steps.

COMPETENCE AND TRAINING

[32] In some of ACM's materials the following warning appears:

"Risk warning: there is risk involved when trading Forex, Commodities and CFDs. CFDs are leveraged financial products and it is possible to lose more than the funds you deposit. Please ensure that you fully understand the risks involved. ACM Gold and Forex Trading do not accept any liability for losses."

This is a proper warning as the financial product here is regarded as high risk and not meant for unsophisticated investors who are seeking capital preservation and growth. The returns can be high but the risks are equally high.

[33] Accordingly there was an onus on ACM to train its brokers or “IBs” in the nature of the product and the profile of the investors for whom the investment is suitable. This requires product training so that the broker has the capacity to provide the investing public with full and relevant information about the product in order to make an informed decision. Training also had to be provided on how to carry out needs and risk analyses before recommending this investment to anyone. In short, ACM were obliged to train their IBs so that the latter comply with the Code when recommending or referring customers to ACM.

ACM provided no evidence of this kind of training. Furthermore, there is no evidence of what oversight ACM applied over the activities of their IBs so that one does not have a situation where a welder ends up trading in CFDs with borrowed money.

[34] I noted that the IB Agreement, in annexure D to the agreement, provides for training. However, this is not the training contemplated in the Code; it is a “Technical Introduction Course” focused on promoting the products and understanding the technology employed.

Marketing Forex and trading in CFD require specialized knowledge, experience and competence. From the information before this office, Go Direct had no such competence.

[35] It is thus unfortunate that ACM actively created the circumstances for Go Direct to commit fraud.

[36] It is complainant's undisputed version that he was told he was buying shares with his R70 000. This can only be due to Go Direct and Bezu misrepresenting the facts. This investment had nothing to do with the purchase and sale of shares. In fact, there was no likelihood that complainant could even understand what dealing in shares means, let alone the forex trading being offered by ACM. Furthermore, had Bezu complied with the Code, he would have realised that this investment was inappropriate for complainant's needs and financial profile. However, Bezu was simply committing fraud and had no intention of legitimately applying the Code.

G. LEGAL CAUSATION

[37] I am of the view that ACM is liable in contract, delict and statute for the conduct of Go Direct and their sequelae.

[38] The issue can be stated as follows:

- a) Whether but for ACM's relationship with Go Direct complainant would not have lost his funds; this is an issue of factual causation; and
- b) If factual causation was established, could ACM be expected to reasonably foresee that Go Direct will use its relationship with it to defraud members of the public? This is an issue of legal causation.

c) On the respondents' own version factual causation was established. But for the relationship between ACM and Go Direct, complainant would not have invested his funds through Go Direct.

The issue of legal causation based on the question of indeterminate liability for FSPs for pure economic loss has to be addressed (the remoteness question).

[39] I do not believe that the loss of complainant's funds falls under the realm of delictual "pure economic loss". The respondents' conduct resulted in direct loss of the complainant's capital or property. In this regard see:-

Telematrix (Pty) Ltd t/a Matrix Vehicle Tracking v Advertising Standards Authority SA 2006 (1) SA 461 (SCA).

'Pure economic loss' in this context connotes loss that does not arise directly from damage to the plaintiff's person or property but rather in consequence of the negligent act itself, such as a loss of profit, being put to extra expenses or the diminution in the value of property.

In the event that I am incorrect (and I do not concede this) in finding that the complainant's loss is not "pure economic loss"; I deal with legal causation in the paragraphs that follow.

[40] ACM merely points out that they had no relationship with complainant, who was not a customer. However, it is easily established that but for the IB Agreement with Go Direct, the latter would not have had the scope and opportunity to commit the fraud. It can equally be said that but for ACM's conduct, complainant would not have invested and would not have lost his funds. Had ACM carried out the inquiries

suggested above, they would have realised that Go Direct were not the people they should be having a relationship with. They were not licensed and lacked the capacity and integrity to be appointed as being fit and proper to serve as IBs. In addition, ACM had insufficient safeguards against director misconduct at Go Direct.

[41] The enquiry is whether, as a matter of public and legal policy, it is reasonable, fair and just to impose legal responsibility for the consequences that resulted from the conduct of ACM in entering into an IB Agreement with Go Direct in the absence of any due diligence?

[42] It is easy and convenient to impute loss to director mismanagement and fraud. The complainant's loss was not caused solely by management failure and/or fraud. If ACM did their work according to the Act and Code, no agreement would have been entered into with Go Direct. The cause of complainant's loss was the inappropriate relationship between ACM and Go Direct. ACM cannot merely ignore the Act and Code and conveniently blame fraud and walk away. Nor can they walk away from the fact that they chose to engage with an entity that was unlicensed in the first place.

[43] The reasonable foreseeability test did not require that the precise nature or the exact extent of the loss suffered or the precise manner of the harm occurring should have been reasonably foreseeable for liability to result: it was sufficient if the general nature of the harm suffered by the complainant and the general manner of the harm occurring was reasonably foreseeable. A skilled and

responsible FSP, acting according to the Act and the Code, would not have formed any relationship with the likes of Go Direct. See:

STANDARD CHARTERED BANK OF CANADA v NEDPERM BANK LTD 1994 (4) SA 747 (AD).

[44] It was also held in the above case that:

“as to the issues of loss and causation, that although the untrue report issued by the respondent had been a factual cause of the appellant's loss, the test to be applied to the question whether the furnishing of the untrue report had been linked sufficiently closely or directly to the loss for legal liability to ensue was a flexible one in which factors such as reasonable foreseeability, directness, the absence or presence of a novus actus interveniens, legal policy, reasonability, fairness and justice all played a part.”

It is appropriate to point out that in addition to these factors one has to take into account, in the circumstances of this case, that there is the Act and Code which all FSPs are bound to comply with as well as legal and public policy. All of which factors, when taken into account in this case, show that there is a sufficiently close connection between ACM's relationship with Go direct and the loss of complainant's capital.

See:

LIVING HANDS (PTY) LTD AND ANOTHER v DITZ AND OTHERS 2013 (2) SA 368 (GSJ);

LEE v MINISTER FOR CORRECTIONAL SERVICES 2013 (2) SA 144 (CC);

STELLENBOSCH FARMERS' WINERY LTD v VLACHOS t/a THE LIQUOR DEN
2001 (3) SA 597 (SCA);

SMIT v ABRAHAMS 1994 (4) SA 1 (A);

ACS Financial Management CC and another vs Coetzee FAIS 00943/10-11/GP.

[45] I accordingly conclude that, based on the peculiar facts of this case, both factual and legal causation was established.

[46] I also point out that the Act and Code must be interpreted and applied in the spirit of the Constitution and the objects of the Bill of Rights. See:

CARMICHELE v MINISTER OF SAFETY AND SECURITY AND ANOTHER
(CENTRE FOR APPLIED LEGAL STUDIES INTERVENING) 2001 (4) SA 938
(CC)

SECTION 27 NOTICE

[47] As indicated above, a notice in terms of section 27 was delivered to ACM wherein an explanation was called for in respect of a number of issues. Some of these questions were answered in their response whilst other questions were evaded.

The following was evaded:

- a) ACM failed to fully address the question why it contracted with an unlicensed entity;
- b) Failed to explain what measures were put in place to ensure that instances of alleged fraud did not occur;
- c) What was the practice between ACM and Go Direct regarding the receipt and depositing of client funds;

- d) An explanation as to who gives advice to complainant on how the company works including but not limited to the process and trade;
- e) An explanation of and disclosure of the policies and processes employed by ACM to ensure fraud and financial loss is prevented in compliance with section 11 of the Code.

Not surprisingly, a vague response was obtained from ACM. They merely quoted the relevant provision of the code without explaining how they complied with it.

FINDINGS REGARDING ACM RELATING TO THE ACT AND CODE.

[48] In all the circumstances and based on the undisputed facts before me; I make the following findings against ACM:

- a) ACM breached Section 7 of the Act;
- b) ACM breached Sections 2, 3(1), 3A (2), 4, 5, 7, 8(2) and 11 of the Code.

H. QUANTUM

[49] There is no prospect that Go Direct and its directors will refund any part of complainant's money. The total amount of the investment is R70 000 which was paid by complainant on the 18th November 2012.

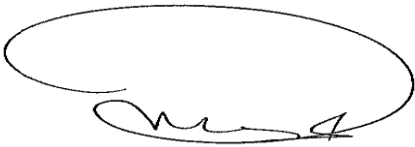
[50] ACM and Go Direct are jointly and severally liable to complainant for the whole amount plus interest.

I. THE ORDER

[51] In the premises I make the following order:

1. The complaint is upheld;
2. Respondents are ordered to pay to complainant, jointly and severally the one paying the other to be absolved, the amount of R70 000.
3. Interest on this amount at the rate of 10.25% per annum from 18th November 2012 to date of payment.

DATED AT PRETORIA ON THIS THE 29th DAY OF JULY 2016



NOLUNTU N BAM

OMBUD FOR FINANCIAL SERVICES PROVIDERS