

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

**PRETORIA**

**Case Number: FAIS-00798/10-11/ WC 1**

**In the matter between:**

**HANNES WATERBOER**

**Complainant**

**and**

**AUDENBERG VERSEKERING MAKELAARS BK**

**First Respondent**

**TOBIAS VAN ZYL**

**Second Respondent**

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**DETERMINATION IN TERMS OF SECTION 28 (1) OF THE FINANCIAL ADVISORY  
AND INTERMEDIARY SERVICES ACT NO. 37 OF 2002 ('FAIS ACT')**

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**A. INTRODUCTION**

[1] On 11 May 2010, Mr Hannes Waterboer (“complainant”) filed a complaint with this Office against Mr T Van Zyl (“Van Zyl”) of Audenberg Versekering Makelaars BK (“first respondent”).

[2] The complaint arises from an investment that was made by complainant in City Capital SA Property Holdings Limited (“City Capital”) on the advice of respondents.

[3] In summary, the complaint is that:

- 3.1. Complainant, despite being a conservative investor, was advised to invest in a high-risk syndication; and
- 3.2. Complainant impressed upon respondents that he was not in a position to lose any money and that the investment chosen had to be carefully considered.

## **B. THE PARTIES**

- [4] Complainant is Hannes Waterboer, an adult male whose details are on file with this Office.
- [5] First respondent is Audenberg Versekering Makelaars BK, a close corporation duly incorporated in terms of South African laws, with its principal place of business situated at 107 High Street, Worcester, Western Cape, registration number (1997/024199/23). First respondent is an authorised financial services provider (FSP) with license number 12619 and was so authorised from 20 October 2004. The license is still in force.
- [6] Second respondent is Tobias van Zyl, an adult male and key individual of first respondent whose address is the same as that of first respondent.
- [7] The Regulator's records indicate that respondents were licensed to render financial services in respect of the product sold to complainant, namely categories 1.8 and 1.10 which relate to the rendering of advice and or an intermediary service in terms of securities and instruments: shares, debentures and securitised debt.

[8] At all material times second respondent rendered financial services to complainant while acting on behalf of first respondent.

[9] In this determination respondent or respondents must be read to mean both respondents.

### **C. COMPLAINANT'S VERSION**

[10] The salient features of complainant's version are set out as follows:

10.1 In May 2007, at the age of 53, complainant gave respondent a cheque to the value of R215 000 to invest on complainant's behalf.

10.2 Respondent invested the R215 000 into City Capital Holdings Limited, (City Capital) to which complainant raised no objections because he had full trust and confidence in respondent's investment acumen. Complainant alleges that he trusted that the money had been wisely invested.

10.3 Less than two years after the investment, complainant received written notification that City Capital had been provisionally liquidated.

10.4 Complainant requested information from respondent regarding the criteria respondent used to "*convince himself*" that the investment in City Capital was a conservative investment.

10.5 Complainant completed a questionnaire before the investment was made, the outcome of which reflected that complainant was a conservative investor.

- 10.6 Complainant argues that his money was placed in a high risk investment. He alleges that respondent reassured him that he had lost nothing by way of invested capital and had only lost the dividends payable to him.
- 10.7 Complainant provided a letter to this Office, which he received from an entity known as Prop@t Investments<sup>1</sup> (Prop@t), after the notification of provisional liquidation of City Capital. Prop@t advised complainant that his investment of R215 000 was worth R79 857, 00 at R0,52 per share, which is R135 143,00 less than the original investment of R215 000, 00. To date, complainant has not seen a cent of his entire investment. He is of the view that he has lost his investment.

#### **D. RESPONDENTS' VERSION**

[11] The salient features of respondents' version are summarised as follows:

- 11.1 On 1 June 2007 complainant sought assistance from respondent to invest his pension fund proceeds. Respondent suggested that a financial needs analysis be done but complainant refused, as set out in the advice record.
- 11.2 Complainant indicated that he had R437 000 available for investment.
- 11.3 Respondent suggested various options. In particular, he suggested that complainant invest R222 000 in Liberty for capital growth and the balance, that is R 215 000, in City Capital, because commercial property was always a good investment considering the annual escalation in rental income as well as appreciation in property. It is common cause that the

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<sup>1</sup> Prop@T Syndications Ltd is a company that received money from investors, in return for shares in the company's various immovable properties. The company experienced financial difficulties and was placed under business rescue effective 29 September 2014.

R222 000 was in fact invested in PIC Investments, also known as Pickvest.

- 11.4 Respondent gave complainant several brochures and explained to complainant the sites of the building, the income generated, the use of the building and the growth potential.
- 11.5 Respondent alleges that complainant accepted the proposal due to the fact that property provided a more stable growth.
- 11.6 Respondent maintains that the outcome of the risk analysis completed indicated that complainant was a moderate risk investor despite complainant's claim that he is a conservative investor.
- 11.7 Complainant was satisfied that it was a five year investment because he only needed the capital investment on his retirement.
- 11.8 Complainant was given a graph which explained the growth of the investment as well as a formula to determine the value of the buildings that respondent recommended to complainant.
- 11.9 Complainant signed the risk disclosure of the application form acknowledging that he had made an informed decision about his investment.
- 11.10 City Capital did not have a registered prospectus because it did not accept investments less than R100 000.

## **E. INVESTIGATION**

[12] The complaint remained unresolved following this Office's rule 6 (b) letter to respondent. On 24 June 2015 this Office referred a notice in terms of section 27 (4) of the FAIS Act, advising respondents that the complaint remained unresolved.

[13] Respondents were invited to provide:

13.1 a statement setting out their case together with supporting documentation;

13.2 evidence, using records compiled at the time, to demonstrate that complainant had been advised of the risks involved in City Capital;

13.3 their record of advice to demonstrate that they had elicited personal and financial information from their client and that they understood their client's circumstances prior to advising him; and

13.4 information which led them to conclude that the City Capital investment was appropriate to their client's risk profile and financial needs.

[14] Respondents were cautioned, *inter alia*, that no *post facto* account would be accepted other than records compiled at the time of providing the financial service to their client.

[15] Respondent in his letter dated 6 July 2015 responded, referring to his previous response and submitting that complainant had not lost any money. Respondent's view was that City Capital was "in a Healthy Financial status with a monthly surplus of income of over R500 000.00 per month after the cost (sic)".

Respondent further complained that 4 years after explaining the situation to complainant, he expected the case to be resolved.

[16] In so far as the request for the records was concerned, respondent simply referred the Office to his earlier response.

## F. DETERMINATION

[17] Section 1 of the FAIS Act defines ‘*complaint*’ as:

*“‘complaint’ means, subject to section 26(1)(a)(iii), a specific complaint relating to a financial service rendered by a financial services provider or representative to the complainant on or after the date of commencement of this Act, and in which complaint it is alleged that the provider or representative -*

*(a) has contravened or failed to comply with a provision of this Act and that as a result thereof the complainant has suffered or is likely to suffer financial prejudice or damage;*

*(b) has wilfully or negligently rendered a financial service to the complainant which has caused prejudice or damage to the complainant or which is likely to result in such prejudice or damage; or*

*(c) has treated the complainant unfairly.”*

[18] In other words, (i) there must be a ‘specific’ complaint (ii) relating to a financial service (iii) rendered to the complainant (iv) by a provider or representative (as defined) and (v) after commencement of the FAIS Act and (vi) the complaint must allege that the act or omission of the provider or representative falls under any one of paragraphs (a) to (c).

[19] Clearly this is a complaint as defined. But is it justiciable?

[20] Rule 4(a) provides that a complaint is justiciable if four conditions are met, namely;

20.1. the complaint falls within the ambit of the FAIS Act and the Rules;

20.2. the person against whom the complaint lies is subject to the provisions of the FAIS Act;

20.3. the conduct complained of occurred at a time when the Rules were in force; and

20.4. the person against whom the complaint lies has failed to address the complaint satisfactorily within six weeks.

[21] The jurisdictional provisions set out in Rule 4 (a) having been met and, owing to the failure by respondents to resolve the complaint satisfactorily, the complaint fell to be investigated. Having fulfilled the requirements of section 27 (4) the Office investigated and completed its investigations.

[22] The issues for determination therefore are:

22.1 whether respondent was in breach of the General Code of Conduct (the Code) in any way in advising complainant to invest in the City Capital investment;

22.2 if it be found that respondent breached the Code, whether such breach caused the loss complained of; and

22.3 quantum.



***Whether respondent breached the Code in any way in advising complainant to invest in City Capital:***

- [23] At the heart of the complaint is the question whether complainant was advised of the risk involved in City Capital, and whether respondent's advice was suitable, bearing in mind complainant's circumstances<sup>2</sup>.
- [24] In the notice in terms of section 27 (4) respondent was requested to provide information which led him to conclude that the City Capital investment was appropriate to his client's risk profile and financial needs. This question requires respondent to have understood the risk inherent in the City Capital investment and match same with complainant's circumstances.
- [25] For respondent to have appreciated the risk inherent in the investment, he ought to have conducted due diligence<sup>3</sup> on City Capital and related entities. In other words, gather pertinent information about City Capital, beyond the statements made by the directors of the company in the advertising material.
- [26] One of the pivotal documents respondent would have needed to refer to is the prospectus. There clearly was no prospectus according to respondent's version. The next question that ought to have come to respondent's mind is how the public property syndication promoter communicated the mandatory disclosures (that had to be made to investors). From respondent's version, it is plain that he had not provided complainant with any document communicating the

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<sup>2</sup> Refer in this regard to the peremptory provision, section 8 (1) (a) to (c) of the General Code.

<sup>3</sup> Section 2 of the General Code of Conduct for Authorised Financial Services Providers and representatives, (the Code) sets out the general duty of a provider as follows: 'A provider must at all times render financial services honestly, fairly, with due skill, care and diligence, and in the interests of clients and the integrity of the financial services industry'

mandatory disclosures. The disclosures are mandated by Government Notice 459, Government Gazette 28690 of 2006, which came into operation on 30 March 2006, (the notice). The language used in the notice is peremptory and must be complied with. In a word, it would be reckless of any provider to advise a client to invest in a public property syndication, without satisfying themselves that firstly, a disclosure document exists and is in line with the requirements of the notice, and secondly, it has been made available to investors.

[27] The mischief aimed at by the legislature is apparent from the content of the notice. The statement is made that the Minister of Trade and Industry, after considering a report by the Consumer Affairs Committee, and being of the opinion that an unfair business practice exists, which is not justified in the public interest, exercised his powers, which led to the publishing of the notice.

[28] Annexure “A” attached to the notice, sets out the minimum information that must be contained in a property syndication disclosure document. Before canvassing the critical provisions of the notice, I pause to mention that from respondent’s own version, there is no indication that he was either aware or had consumed the information in this notice. On this basis alone, respondent could be held liable for advising complainant on this investment. He clearly did not know much about this type of investment, yet he advised complainant that it was stable.

[29] Section 2 of the Notice provides as follows:

‘(a) *Investors shall be informed, in writing, that all funds received from them prior to transfer/finalisation shall be deposited into the trust account of a registered estate agent, a legal practitioner or a certified chartered*

*accountant and provided that such trust account is protected by legislation. Individual investors are to be given written confirmation thereof. It shall be clearly stated **who** controls the withdrawal of funds from that account. Such an account shall be designated " **XYZ Attorneys/auditors/estate agents Trust Account- the xyz syndication**". In the event of investors paying by cheque, promoters shall ensure that the name of the payee is printed in bold on the application forms.*

*(b) Funds shall only be withdrawn from the trust account in the event of registration of transfer of the property into the syndication vehicle; or underwriting by a disclosed underwriter with details of the underwriter; or repayment to an investor in the event of the syndication not proceeding.*

[30] It is common cause that complainant has not seen a cent of his money since he paid City Capital in May 2007. No dividend and no interest payments had ever been made, and this is despite respondent's claims that the entity was in a healthy financial position. Respondent cannot say what happened to the funds. He cannot state whether the syndication did in fact take off. He has not provided a single shred of information indicating whether the property that was aimed at was eventually acquired, the date of such acquisition and the name of the entity within the group, into which the property was registered.

[31] Respondent had not satisfied himself on several fundamental details of a property syndication. I refer in this regard to section 2 (c), (d),(e) and (f) of the notice, which provide:

*c) It shall be disclosed whether the property has been bought conditionally or by option, and in either or both cases full details of any condition and*

*or option on which the property was purchased must be disclosed together with the effective date of commencement of the syndication.*

- d) *Any direct or indirect interest, which a promoter and or any of his/her family member or any other person who is actively involved in the promotion of that syndication has in the property to be purchased, shall be disclosed.*
- e) *It shall be disclosed how any capital shortfall will be dealt with.*
- f) *The method of raising the necessary capital to fund the acquisition of the property and the syndication and how any disbursements will be dealt with prior to transfer, shall be disclosed.'*

[32] These provisions are there for investor protection. Based on the paucity of information that was supplied by respondent to this Office, he would not have known about any conflict of interest concerning the promoter. He had no idea how the syndication and the disbursements were funded prior to the transfer. Respondent was oblivious to these requirements.

[33] There are several other checks that respondent should have covered in his due diligence to satisfy himself about the question of viability of the business proposal. From respondent's version, not much appears to have been covered. Thus, it might prove to be a waste of time to try and canvass all of those elements in this determination. For the sake of time, I will touch on a few issues. Respondent makes no allegation that he had ever perused a set of audited financial statements relating to any of the entities in the group, prior to advising

complainant. It can thus be concluded that the representations<sup>4</sup> respondent made to complainant about the stability of this investment, including the appreciation of property values, were baseless. Without a set of audited financial statements, it is not clear what respondent was relying on when he made the statements about the soundness of the investment. What respondent does not appreciate is that in a business with no effective controls, the values of assets can easily be manipulated and distort the true financial position of the company at any given time. All of this information, is available from a set of audited financial statements, including the auditors' opinion.

[34] Despite being specifically requested to provide information relating to his due diligence, respondent still referred the Office to his submission, which contained voluminous detail of marketing information prepared by the company. Not only is the information worthless, it had no place in terms of informing complainant about the risks involved in the investment.

[35] A further issue which respondent ought to have covered in his due diligence is the question of whether the group complies with sound corporate governance principles. For one, from the publicly available information at the time, there was no independent board of directors exercising oversight over any of the companies of the group. One must emphasise, it is not only a matter of noting that there is a board. The composition and representation on the board is equally important when it comes to good governance. In simple terms, there were no visible means of protecting investors against director misconduct. For

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<sup>4</sup> Refer in this regard to paragraphs 21 and 22 of this determination.

the scale of business respondent was conducting, collecting millions of rand from clients, this ought to have concerned the respondent.

[36] Judging from what respondent furnished to this Office by way of reply, he could not have appreciated the risks involved in the investment. Respondent was in no position to assess the investment for the purpose of advising complainant.

[37] Notwithstanding the aforesaid, careful analysis of respondent's supporting documents is warranted.

### **Risk Disclosure**

[38] In his response, respondent had referred this Office to the risk disclosure notice stating that complainant had signed this document acknowledging that he made an informed decision.

[39] Upon perusing the document, the following were observed:

- (i) the document is half a page;
- (ii) it warns investors to ensure that the investment matches their particular circumstances. Incidentally this is a duty placed on providers who render financial services to clients, in terms of the General Code<sup>5</sup>.
- (iii) the document further goes on to state that City Capital applies gearing;
- (iv) City Capital will obtain up to 70% of mortgage finance which could make the investment sensitive to large interest rate changes; and

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<sup>5</sup> Section 8 (1) (a) to (c)

- (v) it further states that City Capital Financial Services, (CCFS), apparently an associate entity, will charge a performance bonus of 1 % for any share price increase.

[40] A provider acting with due skill and in the interests of his client would have wanted to know the following minimum about CCFS:

- (i) the identities of the individuals behind City Capital Financial Services, (CCFS);
- (ii) the services this entity was rendering to City Capital and the terms thereof; and
- (iii) whether there was any likelihood of conflict of interest between CCFS and City Capital and whether there were any safeguards to protect investors. Respondent does not appear to have concerned himself with this information.

[41] One must accept, since respondent had not made any effort to investigate the governance practices within the group, he would not have appreciated the true extent of gearing by the company and its implications for his client's investment. It is not surprising that respondent had not pointed out these critical aspects of the investment to complainant.

### **Risk Analysis<sup>6</sup>**

[42] Contained in respondent's submissions were copies of the Risk Analysis and Risk Profile documents. The purpose is to demonstrate that the investment was suitable to complainant's risk profile at the time. This is notwithstanding that

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<sup>6</sup> Refers to both the risk profile and risk analysis documents.

respondent had not the slightest clue of what risks were involved in the investment.

[43] Before I deal with the documents I want to first comment on the statement made by respondent that complainant was a moderate and not a conservative investor, as claimed by complainant. Respondent bases his argument on the outcome of his risk profiling exercise.

[44] The risk analysis and risk profiling documents altogether consist of five pages. Several questions are asked. Alongside each question is a score. After answering these questions complainant turned out to be a '*matig*' or moderate investor.

[45] What is known to this Office, which cannot be disputed by respondent of his client is the following:

45.1 At the time of advising complainant, he had accepted a severance package from the Department of Education.

45.2 Complainant was a teacher in what used to be known as Teachers' Training College and had no experience with this type of investment.

45.3 When the Department of Education decided to do away with the teacher training colleges in 2007, complainant opted for the severance pay. At the time it was unclear whether any of the options would suit his personal circumstances, states complainant.

45.4 An amount of R437 000 became payable to complainant and this is all that complainant had at the time.



45.5 Respondent invested R222 000 in PIC Investments and R215 000 into City Capital. Respondent noted this in his advice record.

45.6 Complainant had no other financial arrangements.

45.7 Fortuitously, his mortgage loan (then standing at R172 000) was paid by the Department of Education before paying the lump sum referred to above.

[46] Thus, it cannot be argued, regardless of whatever label respondent assigned to complainant in terms of his risk profiling, that complainant had no capacity to lose his only life savings.

[47] I have gone through the risk profiling document in its entirety. No less than three questions caught my attention:

47.1 Question 5 asks the following of complainant:

*Which one of the following statements best describe the manner in which you earn your income?*

Three choices are offered. The first refers to salaried employees, the second, to self- employed business persons and the third, to the unemployed or retired. Complainant scored the highest score of 6 as a salaried employee. It is not disputed that complainant was unemployed at the time, having taken a severance package.

47.2 Question 10 asks whether complainant expects an increase in his income, (the City Capital investment is excluded).

Three choices are offered. The first suggests an increase in line with inflation with a score of 6.30, the second, an increase that is more than inflation at a score of 9.30 while the last score of 6.00 relates to what is described as, 'reasonably volatile'. The unemployed complainant scored 6.30 for expecting income that is in line with inflation.

47.3 Question 11 requires an answer from complainant as to the size of his income. Four choices ranging between R10 000 and R50 000 are offered. Complainant's income is noted as ranging between R10 000 and R25 000, for which he scored 14.

[48] The entire exercise saw complainant with a score of 62.35, along with the conclusion that he is a moderate investor.

[49] On the basis of the responses to the three questions alone, the entire exercise should be dismissed as irrational. To even suggest that the unemployed complainant was looking at an increase in income that would match inflation is ludicrous.

[50] A responsible provider, acting in his client's interests, would have appreciated that complainant had no capacity to risk his life savings and looked for investments that would preserve his client's capital.

[51] Attached to the risk analysis document is a page with a graph and a simple explanation of the risk involved in the investment. The document first uses a hypothetical scenario to show investors what they can expect in terms of growth on an investment of R100 000, given '*conservative estimates of 7 % rental per annum and an investment capitalisation rate of 8 % per annum*'. The investment

of R100 000 can be seen reaching R261 000 after five years and R876 000 after ten years.

[52] Then this startling statement is made:

*'Risk*

*When we look at the relative risk graph, we find that our product is conservative, shows less volatility than comparable investments but very high returns for the relative risk.'*

[53] Respondent relies, *inter alia*, on this graph to demonstrate that complainant made an informed decision about the investment. It is inconceivable that respondent accepted that an investment with high returns can have conservative risk.

[54] It is clear from respondent's version that he had no clue of the underlying structures of this type of investment, the numerous interrelated entities and other seemingly distant, but connected partners to City Capital like Div-Vest. Given that respondent had not perused a set of audited financial statements and no information regarding the existence of a board, one can rationally conclude that respondent was out of his depth about this type of investment.

### **Advice Record**

[55] I now deal with respondent's record of advice. In his response, respondent made the point that he had advised complainant to do a needs analysis but the latter refused. Nevertheless, respondent provided a document titled Personal Financial Advice.

[56] The document is signed by both complainant and respondent. It records the identified needs as:

*'Clearly a once off investment with Liberty of R222 000*

*An investment with City Capital of R215 000.'*

[57] It is common cause that no investment was made with Liberty; the amount of R222 000 went to PIC Investment Ltd. The rest of the information in this document is unhelpful. How complainant came to have a need such as "*An investment with City Capital of R215 000*", is not explained in the document. Besides, where a client has not provided the necessary details to enable a provider to conduct an analysis, section 8 (4) of the Code applies. Respondent did not supply any record in terms of section 8 (4) of the Code.

***Whether respondent's conduct caused the loss complained of by complainant.***

[58] As a result of respondent's failure to appropriately advise complainant, the latter could not have made an informed decision about the investment.

[59] The letter received by complainant from Progressive Administration (Cape) (Pty) Ltd, (the provisional liquidators) on 5 October 2009 sets out the history of how City Capital [then in provisional liquidation] had conducted itself with investors' funds.

[60] The group whose registered auditors had by then resigned [not before reporting irregularities to several regulatory authorities including IRBA and the FSB] had

no less than six of its subsidiaries finally liquidated and one under provisional liquidation.

[61] The letter further sets out how City Capital had, as early as 2007, in violation of the Companies Act, made several substantial loans to sister entities in circumstances where it could not pay its debts.

[62] City Capital had, without reference to investors, acquired immovable property from related entities and paid monies without conducting the necessary due diligence.

[63] It is a classic story of an entity that was conducted outside of sound corporate governance principles.

[64] One should always be careful of using the benefit of hindsight in these cases. Having said that, there is no doubt in my mind that when respondent advised complainant about the investment he could not have known about the exact details of these poor governance practices. Nor was he expected to foresee the collapse. However, the fact that respondent had not seen a disclosure document that measures up to Government Notice 459, never perused a set of audited financial statements from any of the syndication companies within the group, and could not point to an independent board of directors, should have been sufficient basis for respondent to steer clear of the investment. At the time of advising complainant, respondent had not satisfied himself about the commercial and legal viability of this investment. Quite simply, he had no way of appreciating the risk involved in this investment.

[65] That is not all, respondent was not candid with complainant. A simple statement that he (respondent) knew nothing about investments in property syndications would have sent complainant elsewhere with his money.

[66] It follows that respondent's flawed advice caused complainant's loss.

[67] As to respondent's later suggestion that City Capital is back on track and is in a healthy financial position, it is not surprising that respondent makes this claim without providing any supporting documentation. He made the same irresponsible claims to persuade complainant to buy into this investment in the first place. In fact, Capital Investments, the alter ego of City Capital and where a substantial amount of investors' monies went to, was finally liquidated in July 2009. Respondent does not explain how City Capital would be expected to bounce back into being a viable concern after these major setbacks.

#### **G. QUANTUM**

[68] Complainant invested R215 000 into City Capital following advice of respondent. Of this amount, despite respondent's claims, nothing has ever been paid to complainant. The investment was meant to be five years. It is now four years since the investment matured. In the meantime, there is no credible information to guarantee investors' capital. It is fair to conclude that complainant has lost his capital.

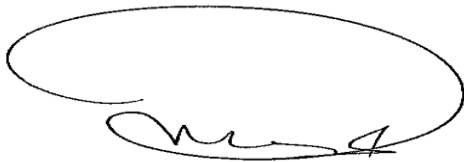
[69] Complainant has asked for relief in the full amount of R215 000.

**H. ORDER**

[70] 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 R215 000. 00;
3. Interest on this amount at the rate of 10.25% from 1 June 2013 to date of final payment.

**DATED AT PRETORIA ON THIS THE 15<sup>th</sup> DAY OF SEPTEMBER 2016**



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**NOLUNTU N BAM**

**OMBUD FOR FINANCIAL SERVICES PROVIDERS**

