To be published by Deon Basson Research CC, 55 Strydom Street,
Birchleigh North, Kempton Park
First Edition: 2008

EDITOR: Chris Davies
COVER DESIGNER: Sybil Basson Smit
**LAYOUT ARTIST: Sybil Basson Smit**

# Chapter 13: The antiquated filing room

*"The factual situation is that the Companies Registration Office has become little more than an antiquated filing room which cannot cope with the demands of modern commerce. The Registrar does not have sufficient staff with the necessary expertise to enable him to carry out functions conferred upon him by the Act and has thus no hope of determining whether a prospectus contains a fair presentation of the state of affairs of the company concerned."* ***–Judge Hennie Nel***[1]

When Sharemax made an elegant side-step into the offices of Cipro[2] (the new name of the Registrar of Companies) in November 2003, the company was supposed to have already been 'converted' to, and have fully embraced the traditions and virtues of company law. For the preceding four years it had escaped the requirement of full financial disclosure by using an unlawful trust structure to raise more than R400m from the public.[3]

I supported Sharemax's move into the ambit of company law in principle[4] but soon realised that Sharemax (as had been the case with PIC Syndications) would take shortcuts and capitalise on the weaknesses in the office of the

---

[1] Nel, Mr Justice H.C. *The first report of the Commission of Inquiry into the affairs of the Masterbond group and investor protection in South Africa,* 1997, vol. 1, p. 40
[2] Companies and Intellectual Property Registration Office
[3] See chapter 5
[4] Basson, Deon. *Sharemax verander ongewone struktuur.* Sake, 17 September 2008 http://www.news24.com/Sake/Maatskappye/0,,6-100_1417758,00.html retrieved on 17 July 2008

Registrar of Companies that had been identified by the Nel Commission in 1997.[5]

"Not only does the Registrar not have an inspectorate with the necessary expertise, he has no inspectorate at all", the commission warned at the time.[6]

It must be understood that Sharemax rolled out new prospectuses at great speed. Subsequent to the 'conversion' in November 2003, R2,8bn was raised from the public through 41 prospectuses. On average this is one prospectus every 6th week. Whoever directly liaised with Cipro on Sharemax's behalf must have been considered part of the family (or mistaken for an employee) in the Registrar's plush headquarters at DTI Campus in Sunnyside.

To register a prospectus is no minor administrative routine. In terms of section 155 (1) of the Companies Act "no prospectus shall be registered by the Registrar unless the requirements of this chapter have been complied with…"

Included in the chapter referred to above is section 148 (1)(a) which requires that every prospectus shall contain "a fair presentation of the state of affairs of the company…" This includes at least the matters specified in parts 1 and 2 of Schedule 3 of the Act.

Now, if one had to cut through the hype of an investment in a property syndication, it is essentially about profitability and the valuation of properties. Profitability is obviously a key determinant of value.

In chapter 7 the legal arguments for and against the disclosure of historic profits in terms of paragraph 6 (h) of Schedule 3 of the Companies Act were presented in some technical detail. Compliance with paragraphs 6 (h) and 26[7]

[5] Nel, Mr Justice H.C, op cit pp. 40-41

[6] Ibid, p. 40

[7] Paragraph 26 requires a report by an auditor where a business undertaking is to be acquired: "If the proceeds, or any part of the proceeds, of the issue of the shares or any other funds are to be applied, directly or indirectly in the purchase of any business undertaking, a report made by an auditor (who shall be named in the prospectus) upon – (a) the profits or losses of the business undertaking in respect of each of the financial years preceding the date of the prospectus; and (b) the assets and liabilities of the business undertaking at the last date to which the financial statements of the business undertaking were made out."

are no minor technical requirements and lies at the heart of profitable and rational investments in property syndication.
Failure to disclose this information is a transgression of section 148 (1)(a) which is an offence. A director convicted of such an offence is liable to be sentenced to a fine or to imprisonment not exceeding two years.[8]
One can also look at this key disclosure requirement from a simple investment perspective, which can best be illustrated with a fictitious example.
Assume a property, operating as a going concern and owned by A, produced profits of R2m, R2,1m, R1,9m, R2m and R2,1m in the five years preceding syndication, and that these profits are duly disclosed in the prospectus.
In the same prospectus B, being the new owner, forecast profits of respectively R3m, R3,3m, R3,63m, R4m and R4,4m for the upcoming five years.
The property is bought from A by B for R20m, and B's holding company C plans to raise R30m from the public through the offer of debentures to fund the acquisition of the property, as well as the lucrative costs related to syndication. The end result is that C has to fund interest commitments on debentures of R30m, although the underlying property asset is, at the outset, only worth R20m.
Based on the big gap between historic and forecast profits and the factual bankruptcy scenario (a property asset of R20m and debenture liabilities of R30m), at least some assertive prospective investors and brokers will ask some probing questions. They are likely to question the huge gap between forecast profits and historic profits, and the pricing of the units to be issued by C (50% premium to the underlying property value). This will in all likelihood lead to firm advice not to invest.
In real life these probing questions are absent from Sharemax syndications since similar disclosures are absent and the investing public is kept essentially uninformed. Cipro

[8] Companies Act, Act 61 of 1973, section 441 (d)

condoned Sharemax's skimpy disclosure philosophy many times by wrongly registering prospectuses that did not contain the disclosures required in paragraphs 6 (h) and 26 of the Companies Act. In doing so Cipro unwittingly became a useful agent for "closed society" practitioners such as Sharemax.

Investors, many acting on the advice of their brokers, were in the same situation as someone buying a horse without knowing anything about the horse's pedigree. It reminds one of Kindersley VC's classic statement:

> "Those who issue a prospectus, holding out to the public the great advantages which will accrue to persons who will take shares in a proposed undertaking, and inviting them to take shares on the faith of the representations therein contained, are bound to state everything with strict and scrupulous accuracy, and not only to abstain from stating as facts that which is not so, but to omit no one fact within their knowledge, the existence of which might in any degree affect the nature , or extent, or quality, of the privileges and advantages which the prospectus holds out as inducements to take shares." [9]

None of the regulators involved with Sharemax can rightfully claim that they had not been alerted at various stages to the pertinent non-disclosure of the information required by paragraphs 6 (h) and 26.

First there was my warning in my answering affidavit: "The non-disclosure is material and there is a direct correlation between profitability and the valuation of properties. Without the profit history of a property it is difficult to assess how realistic profit forecasts are."[10] These court papers were served on the FSB. Other regulators were also alerted.

Then the Prakke report warned about the same issue.[11] Thereafter I reiterated the warning in an article in Auditing SA.[12] Shortly afterwards I was surprised to read the following in a Sharemax newsletter :

---

[9] In *New Brunswick and Canada Rly Co v Muggeridge* (1980) 1 Dr & Sm 363, 381. Quoted in Cilliers H.S. et al. *Korporatiewe Reg.* Second edition, 1992, p. 262

[10] Transvaal Provincial Division of the High Court. *Sharemax Investments (Pty) Ltd vs Deon Basson.* Case number 3208/2006. Answering affidavit by Deon Basson, par. 33.1. Paginated papers, pp. 412-413

[11] Case number 3208/2006. Forensic report by AE Prakke, par. 15.17 to 15.19. Paginated papers, pp. 1114-1115

[12] Basson, Deon. *Who regulates unlisted public offers?* Auditing SA, Summer 2006/7, pp. 9, 10 & 34.

> "Sharemax's compliance awareness week that ran from 1 to 7 February 2007 was a big success. The closing speech was by Mr. Gerry Anderson, deputy chief executive of the Financial Services Board and responsible for the implementation of FAIS, at Sharemax House. It was a privilege to be able to listen to him and he was pleased with Sharemax's role in compliance." [13]

After a while Anderson admitted that he did not make any direct reference to Sharemax whatsoever at the 'Compliance' week. I pointed him to various examples of non-compliance, including failures to comply with the requirements of paragraph 6 (h). I also pointed him again to the Prakke report.[14]

I declared my interest viz-a-viz my litigation with Sharemax and stated: "I understand fully that you cannot get involved in a private legal dispute. Nevertheless, I believe that does not relieve the FSB from its duty to act in the public interest."[15]

To which Anderson replied: "I take issue of the fact that you appear to suggest that my actions are not in a public interest at all times."[16]

Anderson's correspondence led to my letter to the Ministers of Finance and of Trade and Industry.[17] Here the non-disclosure issues again featured. I used the prospectus of Range View Shopping Centre as an example and, among others, raised two simple questions.

**Two simple questions**

- On page 1 it is stated: "The Registrar of Companies has scrutinized the information disclosed in the prospectus". Is this statement factually correct?

[13] Sharemax newsletter, 8 February 2007

[14] Basson, Deon. *The FSB letters.* ITI News, 7 March 2007 See full correspondence at annexure 6 http://www.itinews.co.za/companyview.aspx?cocategoryid=85&companyid=22200&itemid=04F4AC06-627D-4C7F-BEA3-1EF6C88792F8 retrieved on 2 July 2008

[15] Ibid

[16] Ibid

[17] Letter from Deon Basson to Ministers Trevor Manuel and Mandisi Mpahlwa dated 12 March 2007. Published on 24 June 2007 as *An open letter to the regulators*. http://www.itinews.co.za/companyview.aspx?companyid=22200&itemid=E783F28F-5093-4868-B98C-04C37104F5A4 retrieved on 17 July 2008. See annexure 7 for full text of letter.

- According to paragraph 30 on page 29 the following paragraphs (among others) of Schedule 3 of the Companies Act are not applicable: 6 (h) and 26. Why do the Registrar of Companies consider these paragraphs to be "not applicable"? Aren't they vital disclosures?

By August 2008, more than sixteen months after the letter was written, I had still not received any reply from the two Ministers, nor from any regulator. Although all the regulators had been recipients of the letter no-one repudiated my contentions. More seriously, neither did they act. The Registrar of Companies continued to register prospectuses without the required disclosures. And Sharemax retained its status as a Financial Service Provider.

Extreme *laizes faire* thinkers may argue that no harm was done by the non-disclosures, and Sharemax will argue that investors did make profits when it sold certain properties. I will show in appendix 13.1 how investors were prejudiced by the non-disclosures. The problem arose when Sharemax syndications failed to achieve the optimistic profit forecasts in its various prospectuses. This makes Kindersley's earlier statement pertinent.

In understanding what was happening here it is useful to compare the position of a listed company with that of an unlisted company. A listed company will register a prospectus in compliance with the JSE's Listings Requirements. It also has to comply with the Companies Act and its Third Schedule, but in many cases the Listings Requirements will require more information. The prospectus will be analysed by brokers and analysts and soon the market will form a view of the company.

The company will file so-called Sens announcements to keep shareholders updated with material information and reports of pertinent events. This will include profit updates and the publication of results. Thereafter the annual report will be freely and publicly available, making the filing of financial statements with Cipro somewhat academic.

One may very well ask – is it possible for Cipro to impose these same standards on unlisted public companies? The answer is yes and no. *Yes* in that certain disclosures are

mandatory in terms of the Companies Act. As far as that is concerned Cipro has a serious legal duty to maintain high standards. The timeous registration of accurate and complete prospectuses and financial statements are both striking examples.

The answer is also *no* because some companies choose the unlisted route because they know they can get away with substandard disclosure. The fact that currently Cipro is incompetently directed and staffed is an opportunity for fraudsters to prosper.

Willie Botha is a case in point. Practice note no. 1 in appendix 9 to the Companies Act requires that a prospectus contains additional information such as details of relevant previous experience of directors. In relation to Botha's history with DW Promotion and Oude Molen[18], failure to disclose his relevant previous experience is material.[19]

Certainly the FSB and the Consumer Affairs Committee should have passed a note to Cipro about Botha's history when Sharemax went regulator-hopping in 2003. It is rather strange that Botha has, to this day, not seen fit to disclose these details in prospectuses, and it is even stranger that Cipro has done nothing to enforce this requirement.

In 1994, the then chairman of the Standing Advisory on Company Law, Judge Richard Goldstone, addressed the broader issue of compliance in a letter to Trevor Manuel, who was then Minister of Trade and Industry:

> "However, it should be appreciated that if offences of the Companies and Close Corporations Acts are merely overlooked and not prosecuted where necessary, it would simply result in the fact that eventually these two acts would become unenforceable and superfluous. The consequences will be a rapid deterioration of investor confidence, which our country so desperately aspires for at this moment. White collar crime, which has already reached unacceptable proportions, will also escalate." [20]

Judge Goldstone also requested Manuel to consider the appointment of an internal inspectorate in the office of the

[18] See chapter 4

[19] Case number 3208/2006. Deon Basson's answering affidavit, par. 33.5. Paginated papers, pp. 415 & 416

[20] Nel, Mr Justice H.C., op cit, vol. 1, pp. 191-192

Registrar of Companies. It didn't happen. Judge Nel also warned against the dangerous delusion being created that shareholders, investors and creditors are protected by the Registrar.[21]

I've alluded in chapter 7 to Sharemax's shocking stand in 2005 in relation to the filing of financial statements. The fact is that in 2005, for five months after the due date, no financial statements were filed. During that time Cipro failed to make its presence felt by asking for the financial statements, although the debate about Sharemax's non-disclosure was in the public domain.

More than a decade earlier, in 1993, the topic also featured when I addressed an international conference on company law:

> "I do not wish to point fingers but I think the current disclosure requirements of the Companies Act should as a first step be properly enforced before new regulation is dreamed up…the Registrar of Companies or a similar institution should be equipped with the very best staff and technological infrastructure to enforce disclosure. The price tag to this is in my view an essential price."[22]

In fairness I must add that the acting registrar in 2005, Marumo Modiba, was very helpful and treated me with courtesy when I finally approached him after the Freedom Front had handed financial statements to him.[23]

Since 2006 Sharemax has indeed filed some financial statements, but what the real motivating factor might be, I do not know. The pressure factor must have featured in some way. But unlike listed companies, these financial statements are not freely available. Investors are mailed skimpy, abridged financial statements, and if a member of the public is considered to be the "enemy" he or she will have to go through the pain of approaching Cipro. This is in stark contrast with most listed companies where the use of

---

[21] Ibid, p. 189

[22] Basson, Deon. *Openbaarmaking.* Contribution to conference on *The future development of South African Corporate Law.* Delivered at an international conference held by the Coordinating Research Institute for Corporate Law on 28-31 July 1993 at the Carlton Hotel, Johannesburg and organized by the Centre for Business Law, University of the Free State.

[23] See chapter 7

legal technicalities to stymie disclosure is unlikely. Annual reports containing financial statements are in the normal course of events freely available.

Hard copy files of companies' details are supposed to be found in an obscure office block in Sunnyside's Esselen Street and not in Cipro's head office at DTI campus. I've been visiting the Registrar's office since the mid-1980's. In those days it was based in the Zanza building in Pretoria's Proes Street. Getting access to a file was then pretty simple. One paid R5,00 by using a revenue stamp, filled in a form and waited for about 30 minutes in the public area, with dozens of other people who were mainly articled clerks attached to legal firms. No computers were in sight and reference numbers could only be searched by consulting dozens of books which were alphabetically sorted. A clerk would loudly call out your name and you could then read the old-fashioned cardboard-bound file. The contents of the file were, and are literally kept together with infamously pink-coloured ribbon (often referred to as red tape). If it was an old company the file would easily consist of several volumes. If you wished to have copies of any documents it had to be ordered and it could take several days or even weeks to get it.

And if you required a special favour you had to ask the *hoofdame* (chief lady)(a Mrs Brink is one I can remember vividly) who would usually grudgingly oblige.

The culture and atmosphere was distinctly bureaucratic and quality service to customers was not highly valued. By the nature of its activities it was a paper factory par excellence where even the rather primitive technology that was available in the pre-Bill Gates era played second fiddle to manual methods.

Nevertheless, it contributed to South Africa's public record, and in some instances it is and was the only public record of the history of famous and infamous public companies.

In 1998 I ventured the following opinion at a conference on company law in Johannesburg:

> "How cynical you might be about *the public's so-called right to know,* I certainly believe that *disclosure* and the *free flow of information* are the best *checks and balances* in an open society to protect the interests of investors and other stakeholders…The Registrar of Companies, in my book, has for years been a basic contributor to the *doctrine of disclosure*, despite all the criticism levelled at the institution by many observers, including myself. Its structures and resources are far from perfect, but at least we still have an office somewhere in the centre of Pretoria upholding the principle, even if it is only in theory."[24]

By perusing company files I have uncovered many interesting documents over a prolonged period. I'll highlight three fairly representative examples.

In 1985 I found a rather mysterious 'additional page' inserted into the financial statements of Kofkor, an unlisted public company, playing to the sentiments of urban Afrikaners who had a desire to own a piece of a farm. The company made highly optimistic forecasts for its coffee farms in prospectuses and marketing material.[25]

The 'additional page' showed the expenses of the company. Although it was not part of the official financial statements I soon established that it was authentic. It revealed that almost a third of the funds being invested by shareholders were actually being paid out as sales commissions.[26]

The second example is from 2001 when I discovered that the directors of Leisurenet had, long before the listing in 1994, established about 20 unlisted public companies. They raised funds through interest-free debentures from gym members. In fact, the debentures were supposed to ensure gym membership for investors for 40 years.[27]

Instead of using these funds to finance future commitments to gym members, they were swiftly moved out of the public companies, with once-off rental premiums being paid to private entities controlled by the directors.

---

[24] Basson, Deon. *Overcome the traditional bureaucratic approach adopted by the Registrar of Companies.* Paper delivered to Company Law Update. Parktonian Hotel, Johannesburg, 24 June 1998

[25] Meyer, Flip en Basson, Deon. *Kofkor se baas erken daar was foute.* Sake-Rapport, 15 September 1985, p. 1

[26] Basson, Deon. *Die(koffie) pot verwyt die ketel.* Finansies & Tegniek, 17 Januarie 1992, p. 14. Also see chapter 1

[27] Basson, Deon. *Debentures will haunt Health & Racquet members.* Finance Week, 23 February 2001 & *Wealth & Racquet: Illusions of power.* Finance Week , 2 March 2001

On a visit to Cape Town in February 2001 I asked Deloitte & Touche, who'd provided secretarial services to Leisurenet, for copies of financial statements of the various public companies.

They declined, but then presumably felt they had to demonstrate their commitment to compliance, corporate governance, and all the other good business things. They were obliged to make good the 10-year history of non-disclosures by duly filing financial statements for 20 companies for a period of ten years. The pile could easily have filled up a wheelbarrow.

Back in Pretoria I was confronted with loads of paper. I was amused by some freshly stamped financial statements going back a decade. At least I could then follow the suspicious forensic trail of these quasi-hidden unlisted public companies.

The final example is from 1996 when I discovered financial statements for an unlisted public company named Ballito Heights. It didn't raise investments from the public and was in later years converted to a private company. It was, and probably still is, the owner of Dr Louis Luyt's house in Ballito Bay.

The financial statements for 1983 showed that the company spent R667 684 in 1982 and R2,28m in 1983 on improvements to the Ballito property. In those days it was a small fortune and was funded with shareholder loans by Luyt, LLG Beherende Beleggings, other family companies and family members.[28]

Ballito Heights was purportedly registered as a public company to undertake share block developments but these never materialised. The fact that it was registered as a public company made filing of financial statements obligatory until conversion to a private company occurred.

Over time the public area on the 5th floor of the Zanza building became too small and a new and bigger area was allocated on the ground floor. But the number of visitors and

[28] Ballito Heights Limited, Financial statements, 1983

the number of companies registered grew fast. Files could no longer be accessed on the same day they were ordered. Long waiting periods of a week and longer became standard. Fees grew exponentially and the cost to access a hard copy file was, by July 2008, R80.[29]

Commencing during the late 1990's new technology was introduced and big screen computers are now all over the place at both the DTI Campus and the Esselen Street offices. Documents can now be identified on the Registrar's website[30] but the actual physical documents must still be ordered in the old fashioned way.

In 2007 I ordered the 2006 financial statements of the ten Sharemax companies who'd sold their properties to SA Retail. I was told that storing of the physical files had been outsourced to Metrofile and that it would take two weeks to locate them and bring them back to Esselen Street.

Earlier the Registrar's intention was to go virtually paperless and to scan all documents in. I was told by staff members that the scanner had broken in 2004 and has still not been replaced nor repaired.

My request to be informed once the files had been located came to nothing. It was not the first time this had happened.

A customer survey conducted by the Human Sciences Research Council revealed that over half of the employees felt that fraud and corruption were common problems in Cipro. Despite these facts, awareness of Cipro's risk and fraud policy was only moderate with only 49% of employee respondents being aware of it.[31]

Judge Nel believed the most important function of regulating authorities to be the protection of the public.[32] Cipro defines its mission as 'to register businesses and intellectual property rights, to maintain related registries and to]develop

[29] www.cipro.co.za
[30] Ibid
[31] Cipro, annual report, 2007, p. 83
[32] Nel, Mr Justice H.C, op cit, vol. 1, p. 19

information for disclosure to stakeholders'.[33] All very well and noble, but a decisive shift of emphasis to include the words 'public interest' in the mission statement would not be misplaced.

In May 2008 I approached the chief executive of Cipro, Keith Sendwe, directly with a request to make available certain financial statements, in terms of the *Promotion of Access to Information Act:*

> "I treat this as an urgent request for access to the records held by a public body in terms of the Promotion of Access to Information Act because I have in the past on several occasions stringently followed the normal administrative procedures at your office in Esselen Street without any success. The application form in terms of the Promotion of Access to Information Act is attached to the faxed version of this letter."[34]

Sendwe and his staff almost immediately acted positively and within days I had in my possession the copies of 45 of the 60 sets of the financial statements I'd requested .

During that time, but by co-incidence and for totally unrelated reasons, I sought access to the financial statements of Pam Golding Limited, the UK subsidiary of the South African property empire, through the website of *Companies House,* the UK equivalent of Cipro.

It cost me one pound (roughly R15,50) as opposed to R34 per set of financials from Cipro. The transaction with *Companies House* was completed within five minutes, entirely electronically. This, for me, underlined the fact that Cipro still has some way to go if it wishes to emulate international standards.

Financial statements always contain that extra bit of information about a company one didn't know before. It is supposed to be no secret, in fact it is public information. So it was with Pam Golding International: "The company's immediate parent undertaking is Pam Golding International Holdings (Pty) Ltd, a company incorporated in South Africa. The company's ultimate parent undertaking is *The Golding*

[33] Cipro, annual report, 2007, p. 2
[34] Letter from Deon Basson to Keith Sendwe, chief executive of Cipro, 6 May 2008

*Family Offshore Trust*, which is controlled by Dr Andrew Golding."[35]

What secrets would an analysis of the financials of Sharemax syndications reveal?

[35] Pam Golding Limited. *Directors' report and accounts for the year ended 28 February 2007,* p. 11