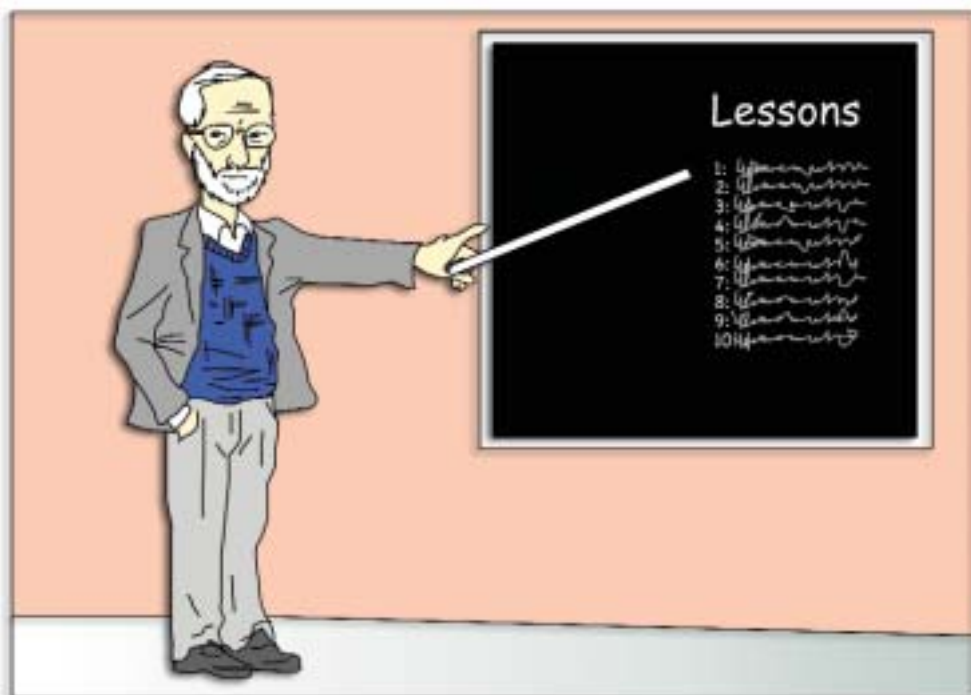


# FAIS Ombud determinations:

## TEN VITAL LESSONS financial services providers cannot afford to miss



*It is still early days, but one thing is absolutely clear – the Office of the FAIS Ombud is determined to protect the consumer.*

In my view, financial services providers (FSPs) will do well to learn from the outcome of the first cases<sup>1</sup> to prevent them from facing the same penalties as the respondents in future. Therefore, this article serves to highlight some of the most obvious issues that the FAIS Ombud, Charles Pillai, regards as absolutely critical as are evident from the recent cases that served before him.

### **1. FAIS Compliance: Operational risk versus advice risk**

The importance of compliance, with specific reference to the advice process and the content of the advice, can never be underestimated and requires a lot more attention. As an industry it is important to differentiate between operational risk and

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advice risk. Whereas the regulator currently mostly monitors operational issues, it is the content of advice that in most cases will be evaluated by the FAIS Ombud. In each of the cases that appeared before the FAIS Ombud, the advice process and the content of advice came under fire. If FSPs aim to succeed in this area, a more focused and well thought through strategy will be required.

### **2. Non-disclosure of relevant and material information will not be overseen**

It appears that the industry is still coming to grips with what is meant by “relevant and material information” with reference to each separate financial need that is expressed by clients. If FSPs are not in a position to define the elements in the advice process that are relevant and material in each case, they must expect the FAIS Ombud to do it for them - unfortunately this can happen only once it is too late to be pro-active. While it seems that the industry is waiting for guidelines from the Office of the FAIS Ombud, Pillai has made it clear that his Office is not an advisory body. Therefore FSPs have no choice but to determine pro-actively what

will be regarded as “relevant and material” before the cases serve before the Ombud in question. I believe there is a lot of work that still needs to be done in this area before FSPs can hope to appear before the FAIS Ombud with some degree of confidence.

### **3. Non-disclosure of fees and/or commission will not be tolerated**

If there is one area in the FAIS Act and its subordinate measures that Pillai has always been very clear on, it is the issue of full disclosures of fees and/or commissions earned by advisers and intermediaries. It will serve all FSPs well to revisit section 7 of the General Code of Conduct for a more comprehensive understanding of these basic disclosure requirements, as I firmly believe that we have not seen the last of the FAIS Ombud in this regard.

### **4. Disclosure of relevant and material information, including fees and/or commission must occur no later than at point of sale**

In order for any client to make a well-informed decision, all relevant and materi-

al information must be disclosed no later than at point of sale. In my view, in practice, the point of sale is when the client agrees to the proposal and signs the application form. It is clear that the following information have to be disclosed to every client at the point of sale:

- The understanding of the client's needs and objectives<sup>2</sup>
- The key features of the proposed product solution<sup>3</sup>
- The specific terms and conditions of the proposed product solution<sup>4</sup>
- The financial service offered by the financial services provider<sup>5</sup>
- The fees/commissions involved<sup>6</sup>

### **5. A needs analysis is non-negotiable**

There is a significant difference between a holistic financial needs analysis and a full needs analysis as prescribed by the General Code of Conduct. It seems that some of the industry players believe that the Act requires a holistic financial needs analysis, where in fact it refers only to full needs analysis.<sup>7</sup> Even a single need requires a full needs analysis with reference to that specific need – not with reference to a holistic financial plan. FSPs will do well to revisit their respective questionnaires in this regard to ensure that they have covered the basic fundamental questions that will be necessary to identify appropriate product(s) in each case.

### **6. The waiver of rights by the client under FAIS is null and void**

Section 21 of the General Code of Conduct is very clear in this regard: "No provider may request or induce in any manner a client to waive any right or benefit conferred on the client by or in terms of any provision of this Code, or recognise, accept or act on any such waiver by the client, and any such waiver is null and void."

In my view, FSPs should steer clear of any form of waiver in the advice process. It is well known that sports teams that play defensively seldom win their games. A more assertive approach may prove to be much more effective for players in the financial advice and intermediary services league. I would strongly recommend that a sound, basic needs analysis be drafted for the various financial planning, including short-term insurance, disciplines and that providers should not even consider the provisions provided for in terms of the General Code of Conduct.<sup>8</sup>

### **7. There must be sufficient evidence that the client was provided with enough information to make a well-informed decision**

The Office of the FAIS Ombud requires clear evidence in order to make fair decisions. As in all court cases "talk is always cheap, but the proof lies in the evidence". It is very clear that Pillai and his Office will consider all relevant and material information; yet, the party that is in a position to supply them with appropriate recorded evidence will be in the strongest position under FAIS.<sup>9</sup>

Providers must however appreciate the fact that section 8(2) of the General Code of Conduct places a more onerous obligation on them than just providing the client with enough information. I believe that we will in the very near future see a number of cases in which the FAIS Ombud will question whether or not the client could actually understand the content of the advice in the particular circumstances. In this regard, it is important to note that two requirements have to be met before any client would be in a position to make a well-informed decision, namely:

- adequate disclosure of relevant and material information; and
- information provided in a manner that will enable the client to understand the content of the advice.

### **8. If there is a conflict between the FAIS Act and another Act when advice is provided regarding a financial product under FAIS, the provisions of the FAIS Act are likely to prevail**

There may be different interpretations and we may see more debates regarding this finding. However, what is clear is that the FAIS Ombud is taking the task that has been given to him very seriously and FSPs should appreciate that, at least at the out-

set of the FAIS Ombud's existence, a very strict interpretation of the law will reign.

### **9. The recording of verbal and written communication relating to the financial advice is necessary to ensure compliance**

In essence, FSPs will have one chance to make a good first impression on the FAIS Ombud whenever a case appears before him. The best chance to impress Pillai and his team is to demonstrate that appropriate records have indeed been kept as required.

In my view the records relating to the client's instructions or reasonable requests and the records of advice will be vital in order to establish a sound basis for any case. In the absence of these records any FSP will always be on the defense and as a result there will be an excellent chance of the Ombud's decision favouring the client.

### **10. The FAIS Ombud recognises the significance of the contractual relationship between the adviser/intermediary under FAIS**

The law of contract fundamentally underlies all instances of the rendering of financial services under FAIS.<sup>10</sup> This underlying agreement comes into existence through offer and acceptance (irrespective of whether the offer emanates from the client, the adviser or the intermediary services provider).<sup>11</sup>

Despite various articles regarding the significance of the contractual relationship between advisers, intermediaries and their clients, it appears that the industry has in general not truly embraced this tool to establish a sound professional relationship between them and their clients and, consequently, an even playing field under FAIS. In my view, this oversight may return to haunt many FSPs in the future.

- 1) Refer to case numbers FOC 979/05 dated 21 July 2005 and FOC/540/05/KZN/(1) as well as the determination against Rosspen Financial Services issued on 29 September 2005.
- 2) Refer to sections 16(2) of the Act and 8 of the General Code of Conduct
- 3) Refer to sections 16(2) of the Act and 7 and 8 of the General Code of Conduct
- 4) Refer to sections 16(2) of the Act and 7 of the General Code of Conduct
- 5) Refer to sections 16(2) of the Act and 3 and 8 of the General Code
- 6) Refer to sections 16(2) of the Act and 7 of the General Code of Conduct
- 7) Refer to section 8(1)(a),(b) and 8(4) of the General Code of Conduct
- 8) Refer to section 8(4) of the General Code of Conduct
- 9) Refer to sections 16(2) of the Act and 9 of the General Code of Conduct
- 10) Refer to Van Zyl in Swanepoel *Comply like a Pro!* 2004
- 11) Refer to Van Zyl *Financial Advisory and Intermediary Services Manual* (2004) Juta pages 1-71