



There are different contracts under FAIS

Different contracts between advisers/intermediaries and clients will play a key role in the outcome of the cases that will be considered by the FAIS Ombud, says Anton Swanepoel, Director: Crux Consulting.

'Financial services in terms of the FAIS Act ... necessarily imply the existence of an agreement or contract between the person who furnishes the advice or renders the intermediary services and a 'client' as defined in section 1(1) of the Financial Advisory and Intermediary Services Act 37 of 2002 (FAIS Act).¹

Different contracts concluded during the various stages of engagement between advisers/intermediaries and clients will play a key role in the outcome of the cases that will be considered by the FAIS Ombud. The aim of this article is to highlight the importance of a basic understanding of the contractual relationship between the parties in terms of the FAIS Act.

The different contracts that are concluded between the parties under the FAIS Act are of vital importance, in view of the common law principles as well as the following sections in the Act and its subordinate measures:

• **Section 3(1)(d) of the General Code of Conduct:**

"The service² must be rendered in accordance with the contractual relationship between the parties and reasonable requests or instructions of the client..."

• **Section 7(1)(a) of the General Code of Conduct:**

"...a provider...must provide a reasonable and appropriate general explanation of the nature and material terms of the relevant contract³ or transaction to a client..."

• **Section 20(3) of the FAIS Act:**

"...the objective of the Ombud is to consider and dispose of complaints in a procedurally, fair, informal, economical and expeditious manner and by reference to what is equitable in all circumstances, with due regard to-

- (a) the contractual arrangement or other legal relationship between the complainant and any other party⁴ to the complaint; and
- (b) the provisions of this Act."

In terms of the above section it is clear that should there be a complaint, the FAIS Ombud Office has to consider the contractual rights and obligations of advisers and their clients, if such a relationship exists. In my view, it is practically impossible for any client to enter into a financial product transaction with a financial adviser and/or intermediary without the establishment of a legal contract between the parties, whether it is concluded verbally or in writing.

As indicated above, it is important to differentiate between the various contractual relationships that may exist between the parties, because the elements of these agreements are quite unique. This is correctly pointed out by Van Zyl.⁵ To differentiate between the various contracts it is necessary to break down the elements in the financial advisory and intermediary services process. In my experience, the following ten elements are present in the business process in an advisory and/or intermediary practice under the FAIS Act:

1. Prospecting for or identifying new clients.⁶
2. Setting up the appointment with the client(s).⁷
3. During the appointment the adviser and/or intermediary normally presents his/her business to the client and tries to establish some form of relationship with the client. There are quite a number of activities during this first interview with the client, ranging from the introduction of the parties, to connecting to each other, to discussing specific business-related needs and objectives. In many cases, at the end of this first meeting, an agreement is

reached between client and adviser and/or intermediary that determines the basis *or terms and conditions of the advisory and intermediary service* that will be provided to the client by the adviser and/or intermediary. This agreement is commonly referred to as the *service level agreement, the terms of engagement or terms and conditions of business*. The elements of this type of agreement are different from the agreement that is reached later on in the process should the client accept the intermediary's proposal.

4. The next step in the process normally involves the gathering of information from the client.⁹

5. Thereafter the adviser/intermediary would continue to prepare the report.¹⁰

6. During the next meeting the adviser/intermediary would present the report.¹¹

7. At the end of the presentation the adviser/intermediary would normally address the main issues (relevant and material information) in the proposal.¹² Section 16(2) of the FAIS Act requires that advisers/intermediaries adequately disclose relevant and material information to clients. At this stage the formal proposal is made to the client. If the client accepts the proposal, another contract would be concluded between the parties. If the client does not accept the proposal there is no consensus between the parties on the essential terms of the proposal and therefore there can be no contract relating to the content of the advice.

8. Acceptance of the proposal.¹³ At this point, a totally different contract, opposed to the service level agreement or terms and conditions of business, is concluded between the adviser/intermediary and the client under FAIS. In this case the parties essentially agree to the *content of the advice/proposal*, which may or may not include elements of a service agreement pertaining to services that may be rendered *after* the financial product is implemented.

Therefore this contract should, in my view, be referred to as the *advice and/or intermediary service agreement* or *an advice record of mutual understanding*. This represents a new type of agreement in the financial services industry in view of its unique elements or *essentialia*.¹⁴

In my view, this agreement should constitute the record of advice as required and referred to in terms of the General Code of Conduct.¹⁵ If one looks at it from a business perspective, it would be wise to ask whether it makes business sense to keep a record of advice without the client's written acceptance of the content of such

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record. Currently, the record of advice is merely an index of procedures followed, without explicitly disclosing the relevant and material information regarding the *content of the advice* as required in terms of the Act.¹⁶

From what I have seen in practice, the current content of most records of advice is totally insufficient to serve as evidence that the provider took reasonable steps to ensure that the client *understands the advice* as required in terms of the General Code of Conduct.¹⁷

It is my contention that the record of advice would be the most important document in the file under the FAIS Act. However, if it is merely a document that is kept in the file without the client's written acceptance, advisers and intermediaries will continue to be exposed under the FAIS Act. In my view, if the record of advice in essence is a recommendation or proposal by the intermediary, which in turn is accepted by the client, a legal contract is concluded and it should be imple-

mented as such in order to serve and protect both parties under FAIS.

9. Implementation of the proposed financial plan.¹⁸ When the insurer accepts the client's application a third contract is established. However, in this case the contract is established between the insurer or the investment company and the client, and not between the client and the adviser/intermediary. In the case of risk business this contract would be referred to as the *insurance contract* and in the case of investments it would be referred to as the *investment contract*.

10. Ongoing advice and management.¹⁹ The ongoing servicing of most clients involves ongoing advice and intermediary services, which are either rendered in the form of advice and/or an intermediary service. Therefore, if anything *material* in the financial plan changes, it changes the content of the advice and intermediary service agreement and it should be amended in order to keep the required records in terms of the General Code of Conduct.²⁰

As indicated above, there are material differences between the typical service agreement/terms and conditions of business, which is normally concluded in the initial stages of the process, and an advice and intermediary service agreement, which is concluded at the *point of sale*. The content and/or relevant and material elements of these agreements are unique.

In my view it is of the utmost importance that all role players in the industry understand and apply the relevant agreements properly, as the law of contract is destined to become the most important instrument to establish a truly fair environment under the FAIS Act for all parties concerned.

¹See Van Zyl, *Financial Advisory and Intermediary Services Manual* (2004) Juta 1-71.

²This service refers to the advice and/or intermediary service that a provider provides under the FAIS Act.

³The reference to relevant contract makes it absolutely vital for advisers and intermediaries to understand which one of the three generic contracts apply during the various stages of the engagement and which elements are relevant and material in each case.

⁴This includes the adviser according to Van Zyl 1-71.

⁵Van Zyl 1-71.

⁶See section 14 of the General Code of Conduct (Advertising and direct marketing).

⁷See section 6 of the General Code of Conduct (Contacting of client).

⁸See sections 4,5, 14 and 15 of the General Code of Conduct (Information on providers).

⁹See section 3(1)(d) and 8(1)(a) and (c) of the General Code of Conduct.

¹⁰See section 16(2) of the FAIS Act and sections 3, 8(1)(b) and 9 of the General Code of Conduct.

¹¹See section 16(2) of the FAIS Act and section 9 of the General Code of Conduct.

¹²See sections 16 of the FAIS Act and 8(2) of the General Code of Conduct.

¹³See sections 20(3) of the FAIS Act and 8(4)(a) and (b) and section 9(1)(c) and 9(2) of the General Code of Conduct.

¹⁴See Van Zyl 2004 1-72.

¹⁵See section 9 of the General Code of Conduct.

¹⁶See section 16(2) of the FAIS Act.

¹⁷See section 8(2) of the General Code of Conduct.

¹⁸See section 2 of the General Code of Conduct.

¹⁹Refer back to the applicable sections in the process above, with specific reference to section 3(1)(d) of the General Code of Conduct.

²⁰See section 9 of the General Code of