FAISOmbud

Office of the Ombud for Financial Services Providers

under the baobab tree

2017 Edition 16

Introduction:

The end of the second quarter of 2017 sees the 16th edition of Under the Baobab Tree, the newsletter of the Office of the FAIS Ombud. The case studies in this edition of the newsletter focus on various areas within the financial planning environment. The first case study deals with credit protection policies, commonly referred to as credit life policies, the second case study looks at endowment policies. The Government Employee Pension Fund and the application of its rules to preservation funds is highlighted in the third case study, and the final case study is dedicated to short term insurance, more specifically homeowners insurance and the perils of not maintaining your property.

Whilst all these case studies differ significantly, the common theme throughout is the requirement that a financial services provider must ensure that he or she obtains all relevant and available information from the prospective client so that any recommendation made is appropriate, and that all material information is disclosed to the client to enable the client to make an informed decision.

Case Study 1: Credit Protection policies

Credit life insurance is the insurance cover that is available to consumers of credit to provide assurance that, in the event of their death, disability, terminal illness or retrenchment - all risks that are likely to impair their ability to earn an income - the outstanding finance charges are provided for. It must be mentioned that in the case of temporary disablement and / or retrenchment, these policies only provide for the payment of the monthly instalments for a period of 6 months. Unlike your more traditional life assurance policies, these policies do not conduct medical underwriting at the inception of the policy, so all applications are accepted irrespective of the risk posed to the insurer. This risk is then subsequently managed by the provision of various exclusionary clauses such as those that deny cover in respect of any pre-existing medical condition that was diagnosed, or for which the consumer received treatment prior to the conclusion of the application.

O vs T:

The Facts:

The complainant had purchased a credit protection policy from the respondent, which incepted on 29 June 2013, subsequent to the complainant having purchased a motor-vehicle. The vehicle had been financed by the respondent and this policy was to have provided cover in the event that the complainant was unable to make the monthly payments as a result of death, permanent disability or retrenchment. Following a stroke, in February 2015, the complainant was rendered disabled as a result of complications from an operation to rectify the effects of the stroke; he then submitted a claim against the policy. In a letter dated 4 August 2015, the complainant was notified that his claim had been rejected as the cause of the disability was directly linked to a condition that had been diagnosed prior to the commencement of the policy. The policy, as the complainant found out, included a 24 month waiting period which excluded any claims related to a pre-existing medical condition that existed prior to the inception of the policy. The complainant had undergone a triple bypass in 1996, and had suffered from high blood pressure since the age of 21. The complainant, who had been medically boarded in February 2015, claimed that despite him having disclosed these details to the respondent's representative, none of these conditions had been captured on the application form, and that no disclosures had been made to him regarding the exclusion of any pre-existing condition let alone the 24 month waiting period applicable thereto.

The complainant approached this Office looking for the disability claim to be settled by the respondent, on the basis that he had never been informed of the exclusions applicable to the policy.

FAIS Ombud's Intervention:

Upon receipt of the complaint this Office directed the matter to the respondent, requesting that it show compliance with Section 8 (1) (a-c) of the General Code of Conduct for Authorised Financial Services Providers and Representatives ('the Code'). This section of the Code specifically requires that a financial services provider obtain all relevant and available information to ensure that not only is the recommendation appropriate to the needs and circumstances of the client, but also directs the financial services provider to make all material disclosures which would enable the client to make an informed decision, a key requirement of the Code. This Office therefore asked the respondent if it had maintained, and was able to provide the required records in compliance with the Code, to prove that attempts had been made to obtain details of the complainant's medical history and to ensure that the relevant disclosures with regards to all the exclusions were revealed to the complainant. This would have allowed him to determine whether he was willing to proceed with the policy despite the 24 month exclusion, or whether he should seek a more traditional life insurance policy that would have conducted the required medical underwriting upfront which, if successful, would have had provided the required assurance in the event of a claim.

The respondent, upon receipt of the correspondence from this Office, revised its decision and decided to honour the claim in full by settling the outstanding finance on the vehicle in the amount of R 115 240.00.

Lessons learnt

1. When you apply for any form of credit, and you are provided with a policy by the representative, you need to determine both the existence and nature of any exclusionary clauses which may result in future claims being rejected as a result of a pre-existing medical condition.
2. There are different types of pre-existing condition clauses which may see the exclusion only applicable for a specified period, e.g. 24 months, or in some cases, this may be a blanket exclusion for the duration of the policy.
3. Should it be that you were previously diagnosed with any sort of medical condition, then having knowledge of the existence and type of exclusion would allow you to determine whether the recommended policy is the best possible solution for your needs and circumstances.

Case Study 2: Endowment Policies

Endowment policies are life assurance products that can hold a variety of underlying investment options, including collective investment schemes (unit trusts). The interest earned by individuals in an endowment policy is taxed within the fund at a flat rate of 30%, which makes them suitable for investors with a marginal tax rate greater than 30%. In addition Section 54 of the Long Term Insurance Act provides for a restriction period during which limitations are placed on the withdrawals you may make from the policy. This applies to the first five years of your policy, where you can only apply for one withdrawal and one loan. Furthermore any additions and/ or amendments made will have the effect of placing the policy into a new period of restriction during which no benefits can be accessed. It is therefore vital that any recommendation with regards to a possible investment into an endowment policy is made only after the financial services provider has considered all relevant and available information to ensure that the recommendation is appropriate.

F v O:

The Facts:

During 2014, the complainant, a 52 year old unemployed female, had approached a representative of the respondent with regards to the options available for her to invest an amount of R200 000. The investment was derived from the proceeds of the sale of the complainant's home, and represented all her capital. The respondent's representative had recommended that she place her funds into an endowment policy and the complainant duly completed the application form provided. Two years after the inception of the policy, the complainant began experiencing financial difficulties, and had approached the respondent with the intention of withdrawing the entire amount from the policy.

Upon consulting with the respondent's representative during September 2016, she was informed that a full surrender of the policy would attract a surrender penalty which the complainant could not afford. The complainant states that she was then given an option to make a partial withdrawal of R50 000 from her investment and that she had completed the relevant withdrawal forms. The complainant had been under the impression that the remainder of the funds would remain intact, and available to her upon request. She was however informed by the respondent that the investment could no longer be accessed and that the remainder of the funds would only be available in 2020 after the policy was placed into a new restriction period.

The complainant does not recall ever having been informed of the penalties and restrictions applicable to this policy, and approached this Office for assistance.

FAIS Ombud's Intervention:

The respondent, in accordance with the Rules on Proceedings of this Office, was provided the opportunity to respond to the complainant's allegations. The respondent indicated (without evidence) that the complainant was aware that her funds were moved from a unit trust to an endowment policy. The respondent advised that all terms and conditions of the endowment policy are provided for in the policy schedule and that that was sufficient disclosure of all relevant information with regards to the product. The respondent also stated that the complainant's signature on the documents demonstrated that the complainant had been aware of the terms and conditions applicable to an endowment policy and had still proceeded with the transaction

This Office was however of the view that regardless of the documentation signed by the complainant, that when one considers the complainant's personal circumstances, it was evident that the product recommended was not appropriate to the complainant's financial needs and circumstances. This Office therefore requested that the respondent reconsider its stance and look to resolve the matter with the complainant. Upon receipt of this Office's recommendation, the respondent made an offer of settlement which was accepted by the complainant.

Lessons learnt

1. Endowment policies, whilst they do provide benefits to individuals with a marginal tax rate in excess of 30% for example, may not be suitable investment vehicles for all investors, especially if you require access to the funds within the initial restriction period.
2. It is important that your financial advisor obtain all relevant and available information from you to ensure that the product that is recommended is appropriate to your needs and circumstances.
3. Ask your financial advisor to explain various investment options available to you, and the advantages and disadvantages of each investment and how they apply to you your specific needs, so that you are able to make an informed decision as to the product that will best suit your needs.

Case Study 3: Government Employee Pension Fund (GEPF) and Preservation Funds

The Government Employee Pension Fund (GEPF) is Africa's largest pension fund; it is a defined benefit pension fund, governed by the Government Employees Pension Law (or GEP Law). The rules of the GEPF differ from private pension funds specifically with regards to preservation funds. A preservation fund, as the name suggests, enables you to preserve your pension fund savings prior to retirement. When one either resigns, is retrenched or even dismissed from your employer, you can transfer the benefits of your pension fund into a pension preservation fund and the proceeds will remain tax free until such time as you chose to make a withdrawal. Prevailing legislation allows for the member of a private pension scheme to make one withdrawal prior to transferring to a pension preservation fund, without compromising the one withdrawal that is available within the preservation fund. At retirement the member may then access 1/3rd of the pension benefit with the remaining two thirds used to purchase an annuity to provide an income for life. The rules of the GEPF, however, do not permit a member to access any funds prior to the transfer to a pension preservation fund. Whilst in the preservation fund, the member may make withdrawals which are limited to 1/3rd of the benefit amount. Furthermore, at retirement the member does not have access to the 1/3rd of the investment and the entire benefit is used to purchase an annuity. It is therefore vital that those withdrawing from the GEPF ensure that they are appropriately advised of the options available.

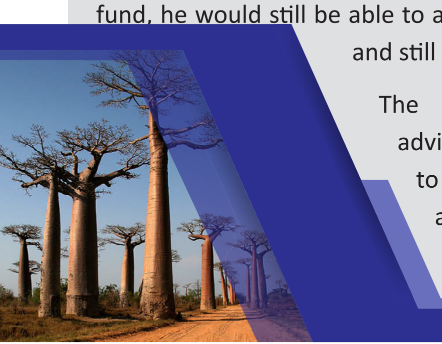
P v O:

The Facts:

The complainant, who was 48 years old when the application was concluded, had been employed with the SANDF for 29 years. The complainant decided to resign from the SANDF to pursue an alternative career, and had required the proceeds from his pension fund, an amount of R2 841 364.86 to purchase an existing business. The complainant had, upon his resignation, approached a representative of the respondent for advice on accessing R2 100 000 of his pension fund benefit in order to buy the business. A representative of the respondent, however, informed the complainant that he would incur a heavy tax burden should he access the funds directly from the GEPF. The complainant informed the respondent's representative that he was prepared to pay whatever tax was applicable, as he needed the R2 100 000, which had been the sole reason for his resignation. However, the representative had been adamant that by transferring his pension fund benefit to a preservation fund, he would still be able to access the required R2 100 000 and still preserve the remaining funds.

The complainant accepted the advice provided, and subsequent to the transfer of the funds to a pension preservation fund, and completion of the withdrawal forms, the complainant was advised that his withdrawal was limited to 1/3rd of the pension benefit, an amount of R947 121.

Despite numerous attempts to resolve the matter with the respondent failed to bring about a resolution, the complainant approached this Office for assistance.



FAIS Ombud's Intervention:

Section 8 (1) (a) of the Code provides that all relevant and available information must be obtained from the complainant to ensure that the recommendation is appropriate to the needs and circumstances of the client, in this case the complainant. It is not in dispute that the respondent's representative had been aware of the complainant's objective of purchasing a business as well as the amount that he required. Having therefore been provided with this information which was relevant to the complainant's situation, and freely available, the representative nevertheless failed to act with the required due skill care and diligence with a recommendation that prevented the complainant from achieving his desired outcome - to purchase a business.

When this was put to the respondent, a decision was made to resolve the matter in full and final settlement of the complaint, and an offer was presented to the complainant that was ultimately accepted.

Lessons learnt

1. The rules of a pension fund will always supersede prevailing legislation, and you need to ensure that you acquaint yourself with the rules applicable to your pension fund in case you have cause to withdraw from the pension and/ or provident fund prior to retirement.
2. This becomes all the more important when one resigns from ones employment with the specific objective of starting or purchasing a business that may require accessing the capital as a withdrawal benefit.
3. The decisions one makes upon withdrawing or retiring from a retirement fund can have significant and lasting consequences, so it is vitally important that you ensure you receive appropriate advice and that your decision meets your specific needs.

Case Study 4: Homeowners Insurance

Generally, the higher the potential return of an investment, the higher the risk. It must be appreciated that there is no guarantee that you will actually get a higher return by accepting more risk. It is for this reason that the old adage of diversification, which is the spreading of your portfolio between various asset classes, enabling you to reduce the risk of your portfolio without sacrificing potential returns, still remains relevant. Once your portfolio has been fully diversified, you can then look to assume additional risk in certain areas should you be required to earn a higher potential return on your portfolio. At the end of the day, you must realise that one size does not fit all, and regardless of your attitude towards risk, the risk that you need to take for a specific investment needs to be considered for different investing stages and for different goals and objectives.

N v S:

The Facts:

On 24 July 2014, the complainant applied for a home loan as well as a homeowner's insurance policy with the respondent. During November 2016, the area where the complainant lived experienced heavy thunder storms which resulted in damage to the complainant's property. The complainant lodged a claim with the respondent for damage sustained to the floor and to the roof of the building. On 20 January 2017, the complainant was informed that the claim for the floor had been approved, but the respondent refused to repair the roof which they said had been damaged as a result of poor maintenance. The complainant was dissatisfied with the outcome of the outcome of the claim, saying she had not been informed of this exclusion upon applying for the policy and had thus been denied the opportunity to undertake the required repairs.

FAIS Ombud's Intervention:

In answering the initial correspondence from this Office, the respondent claimed that the policy had been sold without advice and that it had been sold solely on features and benefits. The respondent therefore remained adamant that it would only settle the claim with regards to the damage sustained to the floor. Prior to the matter being formally accepted for investigation, this Office made a recommendation to the respondent for the matter to be settled. The letter of recommendation reiterated that financial services cannot be provided without the provision of advice. Furthermore the exclusion that pertains to the failure to maintain the property was a material term of the policy that was required to have been disclosed in terms of section 7(1) (c) (vii) of the Code which requires that concise disclosures be made of any exclusions, and or circumstances in which cover will not be provided. There were no documents proving that the respondent had complied with this section of the Code. Had such a disclosure been made, the complainant would have been in a position to make an informed decision and would have been able to mitigate her losses. The respondent subsequently approached the complainant and proposed a settlement offer of R 166 830 in full and final settlement of the claim. The complainant accepted the offer.

Lessons learnt

1. When purchasing a new property it is important to familiarise yourself with the state of the building to determine when maintenance had last been carried out by the previous owner.
2. A short term insurance policy will not provide cover in instances where a building or property has not been adequately maintained regardless of whether the lack of maintenance was occasioned by the policy holder or the previous owner of the property.

FAIS Ombud Graduate Trainee Program

The FAIS Ombud Graduate Trainee Programme was established in December 2010 with the aim of grooming promising law graduates from previously disadvantaged communities and institutions through mentorship and training for a period of 12 months. Candidates are selected from various law schools and as a requirement, must be in the process of completing their Practical Legal studies. The programme has since launched the careers of 43 Graduate Trainees and continues to afford selected law graduates the opportunity to kick-start their careers in a high performing professional environment while gaining exposure to various legal aspects in financial services. The programme continues to mature, and a growth in the number of graduates joining our organisation every year signifies the development of the programme as well as the confidence of the FAIS Ombud in the benefit accrued by each graduate at the end of the 12-month period.

The training covers topics such as investments, financial services legislation and retirement planning as well as soft skills; all assisting graduates to be successful in their future endeavours. We are confident that the programme contributes to the wider economic development of South Africa.

This Office would like to congratulate Mr Andani Komeni, Ms Tshilidzi Nemaonzeni, Mr Tumelo Letaoane and Ms Olwethu Mnguni the successful candidates following the recruitment drive which was concluded during June 2017. These candidates entered the program on 1 July 2017 and we wish them all the very best.

Mr Andani Komeni, Ms Tshilidzi Nemaonzeni, Mr Tumelo Letaoane and Ms Olwethu Mnguni

Determinations:

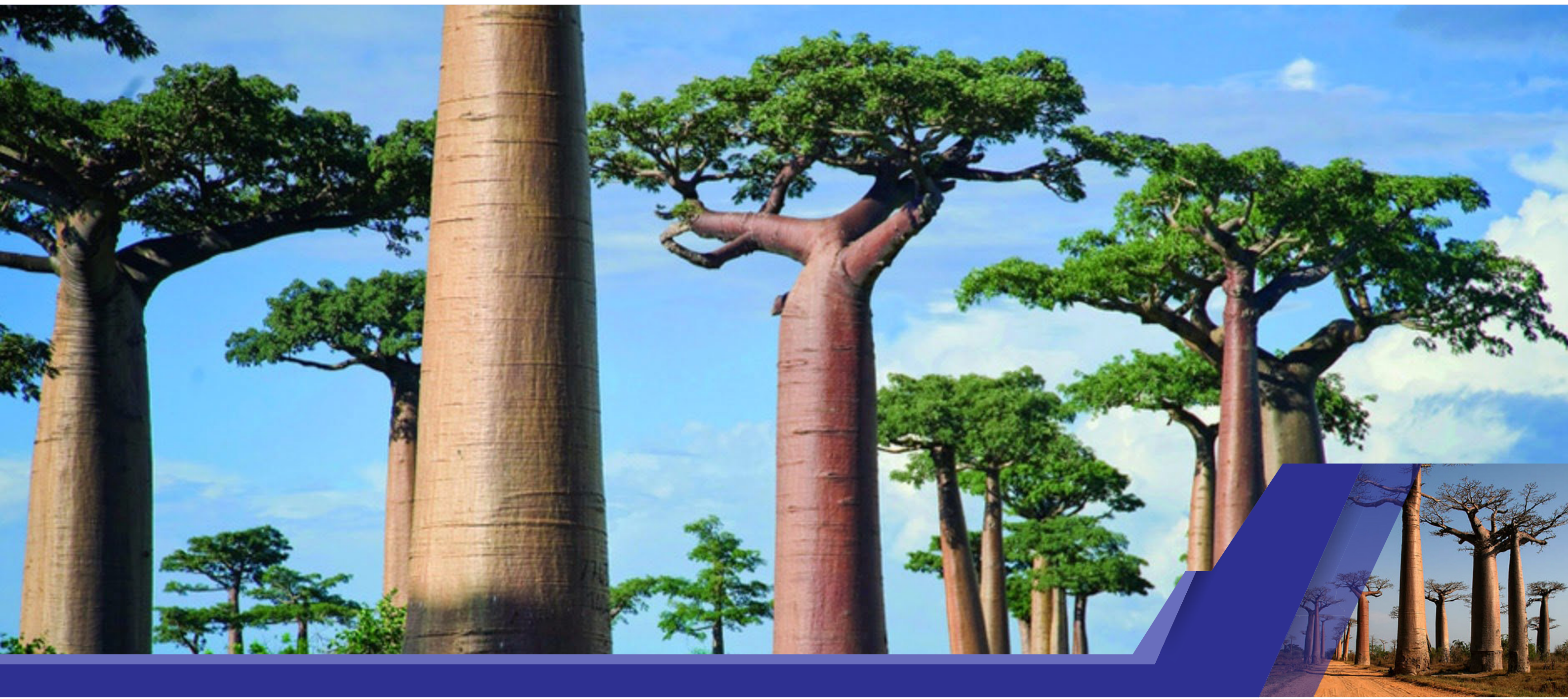
In terms of Section 28 of the Financial Advisory and Intermediary Services Act, where a matter has not been settled or the FAIS Ombud's recommendation not accepted by the parties, the FAIS Ombud will make a final determination which may include –

- the dismissal of the complaint; or
- the upholding of the complaint wholly or partially, e.g. by awarding the complainant an amount as fair compensation for the financial prejudice or damage suffered.

Determinations issued by this Office provide valuable insight into the manner in which this Office interprets the provisions of the FAIS Act and its corresponding General Code of Conduct for Authorised Financial Services Providers and Representatives.

Below is a table of all determinations issued during the quarter January 2017 to March 2017, and are available on our website at www.faisombud.co.za.

Year	*Product*	*Complainant*	*Respondent*	*Date issued*
2017/18	Investments	TEDDY MADITSE	MAGAJANA TRADING AND PROJECTS CC & LINDIWE MTASA MAGAJANA	**201706/06**
2017/18	Long-term	HYLTON FORGE	OLD MUTUAL LIFE ASSURANCE COMPANY & SOUTH AFRICA LIMITED (OMLACSA)	**201705/22**
2017/18	Long-term	Babalwa Molate	Discovery Life Limited	**201705/05**
2017/18	Investments	Melany Deborah Anne Koekemoer	JAM Financial Planning CC & Willem Johannes Abraham	**201705/05**
2017/18	Investments	Tielman Dreyer Odendaal	JAM Financial Planning CC & Willem Johannes Abraham	**201705/05**
2017/18	Investments	Amandus Tobias Viljoen	Dawie Joubert Versekerings Makelaars BK & Dawie Joubert	**201704/24**
2017/18	Investments	Cornel Erasmus	Dovetail Trading 509 cc & Hermanus SP Lombaard	**201704/10**



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Anyone who has a complaint about the service delivery of this office must kindly email their complaint to hestie@faisombud.co.za