



Introduction:

The end of the first quarter of 2017 sees the 15th edition of Under the Baobab Tree, the newsletter of the Office of the FAIS Ombud. The theme of this newsletter is focused on investment planning, an important aspect of any financial plan whether your investment goal is to own your own home, higher education for

your children, a new vehicle, or simply saving for a rainy day. It is vital that you clearly communicate your goals and objectives to your financial advisor who also has a responsibility to obtain all relevant information to ensure that any recommendation made not only allows you to achieve your goals, but also suits your current financial needs and circumstances.



Case Study 1: Guaranteed Income Plans

Many insurers have products usually referred to as 'Guaranteed Income Plans'. These plans are made up of two policies, an endowment policy which provides a return of the capital invested after a five-year period and a temporary life annuity policy provides a five-year fixed monthly income (illustrated below). Potential clients need to be wary: these guaranteed income plans come in two different formats, one option pays a specific income and guarantees the capital after 5 years; the other option, whilst providing a slightly higher monthly income, does not guarantee the capital. The funds placed in 'Policy 2', shown in the illustration below, are invested in the markets with the hope that the maturity value either equals or exceeds the original capital after 5 years. Both options have their pros and cons, and as always, the most suitable option would depend on the client's financial needs and circumstances at that time.

Combined Policy Investment of R100 000	
Policy 1 5 Year temporary annuity R22 790.90	Policy 2 5 Year endowment R77 209.90
Payment of R (Annuity Income) For period of 60 months	Guaranteed Maturity Value R100 000

The Facts:

This Office received a complaint from a father acting in his capacity as the guardian of his 47 year old daughter who lacked the mental capacity to represent herself. Owing to the daughter's mental illness she had never been employed and was dependent on the support provided by her then husband. The daughter and her husband subsequently divorced. As part of the settlement, the daughter received a house which was later sold for R2 100 000. The proceeds were subsequently placed in a family trust, with the intention of investing the monies in a vehicle that will protect the capital and provide monthly income payments to sustain her. Upon meeting with the respondent, the recommendation was made to invest in a guaranteed income plan which guaranteed her an income for a period of 5 years. The complainant, representing the daughter, accepted the recommendation, only to find that at maturity, the original capital amount was not guaranteed and that payment would be less than what was originally invested.

Upset that the instruction to guarantee the capital had not been adhered to, the complainant lodged his complaint with the FAIS Ombud.

FAIS Ombud's Intervention:

The information provided to this Office by the respondent in reply to our initial correspondence was that the complainant had

signed the application and the quotation in acceptance of the recommendation made. Furthermore the respondent was of the view that the matter related to the performance of the funds into which the capital had been invested. The respondent was also of the view that the complainant had in fact not suffered a loss, as when one added the total of all the instalments paid to the complainant, with the capital paid at maturity, it was more than what had been originally invested. This Office was not convinced and was of the view that the respondent had failed to adequately consider the complainant's financial needs and circumstances at that time, and had therefore failed to provide her with a product that was appropriate. I would add that the respondent had failed to render the financial services in line with the terms of the agreement with the client. A recommendation was made to the respondent to resolve the matter with the complainant, which was followed by an offer from the respondent to resolve the matter with the complainant. The complainant duly accepted the offer in full and final settlement of the complaint.

Lessons learnt

1. Guaranteed income plans, as the name suggests, provide a guaranteed income for a period of 5 years. Upon maturity, and depending on the option chosen, the insured will either receive the original capital if it was guaranteed alternatively, if it was not guaranteed, the insured could receive either more or less than the capital originally invested depending on the performance of the markets.
2. The difference between the guaranteed option and the option without a guarantee has a direct bearing on the level of income one will receive. There is a cost attached to the guarantee of capital and it will often result in a lower income.
3. Clients need to be informed of both options together with the pros and cons of each and how they relate to their individual financial needs and circumstances, so that they make an informed decision in choosing the options.



Case Study 2: Endowment Policies

An endowment policy, contrary to the casual references that it is an investment, is in fact a life assurance contract which is designed to pay a tax free lump sum after a specific term, the minimum being five years. In accordance with Section 54



of the Long Term Insurance Act, the 5 year minimum term is referred to as a restriction period and during this period the policy holder has only two options with regards to accessing their funds namely: one loan and one surrender. Section 54 restricts endowment policies with regards to the minimum term and accessibility of the funds invested. In addition, should the premiums increase by more than 20% compared to the aggregate premium paid during the last two premium periods, a new 5 year restriction comes into effect. These restrictions require that serious consideration must be given to determine whether this product meets with one's specific circumstances.

The Facts:

During 2015, the complainant sought the respondent's assistance in order to invest the proceeds awarded to her by the Road Accident Fund (RAF). The claim with the RAF was as a result of an accident that had left the complainant paralysed. The complainant claims to have specifically requested an investment product that would provide her with a monthly income without eroding her investment capital. The complainant alleged that she was advised by the respondent to place her funds into a unit trust which would provide her with the required monthly income from the product's accumulated interest. The respondent further promised that there would be no fees charged should the investment be cancelled.

The complainant however, did not receive the promised monthly interest for a period of approximately six months resulting in the respondent recommending that the complainant move her funds to another investment in an effort to meet her income needs. When the second investment also failed to provide the required income, the complainant decided to cancel the investment with the respondent only to discover that her funds had been invested in a five year endowment which she could not cancel without sustaining significant penalties due to early cancellation.

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 are provided for a specific term, the minimum of which is five years. During this term the investor is restricted with regards to accessing the proceeds thereof. Prospective clients should therefore thoroughly consider the appropriateness of this product if they anticipate the possibility of needing to access the funds within the restriction period.
2. It is vital for a Financial Services Provider to take into consideration the client's needs and circumstances when recommending and implementing financial products to ensure that these needs are met.



Case Study 3: Effects of fees and charges

Costs have a dramatic impact on one's long-term savings outcome. But this only becomes obvious once fees are seen in their proper context. Take this example, in which an investor puts R500 away each year for 30 years, depositing a total of R180, 000 over that time:

Average Annual Return	Total Annual Investment Fees	Value after 30 years	Amount lost to fees
7%	0%	R588,032.77	R0
7%	0.25%	R561,515.53	R26,517.24
7%	0.5%	R536,320.22	R51,712.44
7%	1.0%	R489,628.12	R98,404.65
7%	1.5%	R447,454.73	R140,578.04
7%	2.0%	R409,348.84	R178,683.93

Financial Services Providers therefore have a duty to not only disclose any fees and charges payable by the client, in monetary terms, but must also provide clients with the option to negotiate any



fees if possible such as commissions payable to the provider, as they can have a significant impact on the outcome of ones investment at maturity.

The Facts:

The complainant, an elderly gentleman in retirement, submits that he had invested an amount of R1 000 000 in a fixed deposit on the advice of the respondent's representative. When the fixed deposit had matured, the complainant had been referred to another representative of the respondent, who asked for details with regards to the income he was receiving from his fixed deposit. When the complainant advised he was earning 9.8%, the representative had advised him that if the complainant moved his portfolio to her, where it would be invested into a basket of unit trust funds, then he would be able to take home a 10% monthly income together with a 5% growth on his investment. The complainant contends that he had made it clear to the representative that the investment had to last him for the rest of his life as it was his only source of income, and he had been assured that his money would be safe.

The complainant submits that since he was not too familiar with investments, he had requested a weekly statement in order to see how the investment was doing. Soon after the investment had incepted, the complainant became weary of losses being sustained on the portfolio, and despite having approached the representative on a number of occasions to express his concerns with regards to the depreciating value of his investment, there appeared to be no appreciation for his concerns. The complainant submits that as a result of his portfolio having reduced by around R70 000, due in part to the representatives commission which had been in excess of R11 000, he was worse off than before, and had decided to withdraw all his money and had once again invested into a fixed deposit.

FAIS Ombud's Intervention:

On receiving the complaint, this Office addressed a letter to the respondent. In answer to our initial correspondence the respondent alleged that the complainant had been advised of the depreciation that would occur due to the high income drawdown required by the complainant. It is further alleged that the complainant had been made aware that the investment would only start to show significant gains after a period of 3 to 4 years. The respondent further submitted that the complainant had not incurred any loss, as one needed to consider that the monthly income already received together with the capital amount withdrawn by the complainant had exceeded the funds initially invested. This Office was however of the view that when one considered the complainant's age, the lump sum involved, the fact that this was his only source of income and his inability to recoup any losses sustained, that the respondent's representative should have exercised greater caution and ensured that the complainant's capital was at the very least preserved. Furthermore the duty of a

Financial Services Provider is to provide advice and not simply accede to the complainants wishes especially when these 'wishes' are in conflict with his circumstances. This was true for this matter where the respondent had allowed the complainant to draw an income of his choosing without ever cautioning him as to the risks involved.

The respondent there and then made an offer in full and final settlement of the matter, and the complainant had accepted the offer.

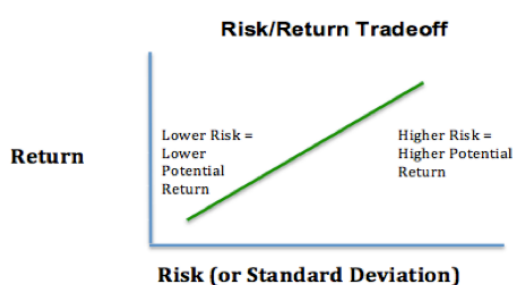
Lessons learnt

1. When drawing an income from an investment you must ensure that the percentage being drawn as an income does not exceed the percentage return being received from the funds invested into. If the level of income is too high then one runs the risk of diluting the original capital which is not only very difficult to recoup, but will begin having an effect the ability of maintaining the level of income. The importance of extracting relevant information from a client to understand their needs is crucial to ensure that whatever advice is given to the client suits his or her needs.
2. If the income you are drawing is for retirement, and one has not made sufficient provision then it is important that you, have a serious discussion with your Financial Services Provider with regards to not only the level of income to be drawn, but also the risk that you would need to assume to provide for the income drawn. For example a conservative investor may need to either consider assuming greater risk, or make provision for a reduced income.
3. A Financial Services Provider is unable to rectify a situation where you have not made sufficient provision for retirement; however there is a duty to ensure that what funds are available, are utilised effectively to ensure that the client receives an income for life.



Case Study 4: Risk vs Return

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.



The Facts:

The complainant, 59 years of age, approached the respondent's representative to discuss a possible switch of her funds held in a money market account into a portfolio that would potentially provide a higher return. The complainant informed the representative that as a result of her age, she could not afford to lose any money and that she was dependant on these funds to provide an income for retirement. The respondent's representative then conducted a risk profile, and a needs analysis which portrayed the complainant as a moderate risk investor. Based on this outcome the respondent recommended that the funds be placed into the respondent's bond fund, with the assurance that she will receive returns on her investment.

The complainant accepted the recommendation, only to later find that her capital had decreased as a result of additional fees and charges she had not been aware of, and she requested that the financial planner switch her funds back into the money market fund.

FAIS Ombud's Intervention:

The complainant approached the office of the FAIS Ombud to request the respondent to place her in the financial position she would have been in had she been advised of the risks involved in placing her money in the bond fund.

This Office directed the complaint to the respondent in accordance with the Rules on the Proceedings of the FAIS Ombud, and in reply, the respondent offered the complainant a settlement which the complainant then accepted in full and final settlement.

Lessons learnt

1. In wanting a higher return clients looking to invest must appreciate that there is a trade-off between risk and return. The higher the desired return, the greater the risk that you must be prepared to assume.
2. There may however be times when you may need to assume a higher risk to attain specific goal. This must be done in consultation with your Financial Services Provider and in accordance with what is appropriate to your situation.



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 received by each graduate at the end of the 12-month period.

The training provided on topics such as investments, financial services legislation and retirement planning as well as soft skills will assist each graduate to be successful in their future endeavours. We are confident that the programme contributes to the wider economic development of South Africa.

During the first quarter of 2017 the Office of the FAIS Ombud once again embarked on a recruitment drive to the various law schools in South Africa, looking for candidates for the July 2017 intake (see photographs below). We shall report back in next quarter's edition as to the successful candidates.



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.

The FAIS Ombud's determination has the effect of a civil judgement of a court.

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. These are available on our website at www.faisombud.co.za.

<i>Year</i>	<i>Product</i>	<i>Complainant</i>	<i>Respondent</i>	<i>Date issued</i>
2016/17	Investments	ABDOL FARO	GROENLAND INSURANCE BROKERS CC & PETRUS SWART	20170328
2016/17	Investments	CAROL CHARLOTTE VAN ZYL	JOHANNES CHRISTIAN MOSTERT	20170324
2016/17	Investments	HUIBRECHT JOHANNA FREDERICKA PFISTER	FREESURE PTY (LTD) and LOURENS OBERHOLZER	20170221
2016/17	Investments	MAGDALENA CV SWANEPOEL	HUIS VAN ORANJE FINANSIËLE DIENSTE BPK & BAREND PETRUS GELDENHUYS	20170131
2016/17	Investments	WAYNE BERNARD KLUG	TRADING TO GET RESULTS CC & PIERRE-LOUIS VAN DER WALT	20170130





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