OPERATIONAL EFFECTIVENESS

ICT Governance

The Audit and Risk Committee monitors ICT governance by considering the efficiency and effectiveness of ICT controls, policies, processes and the associated risks. They also monitor the ICT initiatives in order to detect ICT risks and to recommend mitigation of potential threats to operational continuity and ensure return on investment (ROI).

The FAIS Ombud has adopted technology that ensured better efficiency and improved turnaround time. During the year under review ICT concluded a procurement process to upgrade the legacy core system to latest version. The process of replacing the core legacy system with an effective and efficient complaints handling system that will support the entity core business has commenced.

The common challenge faced by most organisations is lack of cyber security monitoring solutions and measures to mitigate cyber risks. However, FAIS Ombud ICT has ensured that the ICT environment and information system risks are managed and mitigated effectively by putting in place a number of compensating measures during 2019/2020 financial year, including a Security Information Event Management solution and vulnerability assessments that were conducted on a monthly basis. Deficiencies identified were addressed immediately to avoid any potential shortcomings and reduce related risks to minimal.

The ICT department embarked on various initiatives and projects to align ICT to business. The ICT governance framework and ICT strategy were revised to accommodate these envisaged changes.

"Having someone who listens is a great gift, but to be truly heard, is a treasure."

TRENDS

Endowment Policies

The Office of the FAIS Ombud has noted that a majority of complaints with regards to endowment policies emanate from 'causal effects' such as a surrender penalty and the application of restriction periods. Whilst these causal effects only become prevalent at the termination of the policy or when the policy matures, at which point the clients are suddenly faced with surrender penalties and fees that they were not informed of, the main concern for the FAIS Ombud Office is that in most instances the endowment policy was not appropriate to the client's needs and circumstances in any event, and ought not to have been recommended in the first place. The misleading component of endowment policies stems from the manner in which these policies are sold. These policies are in fact sold as investment solutions and savings products, utilising the term investment as opposed to policy, without any emphasis on the fact that they are actually life assurance policies. It may appear to be a fine technical issue but it has significant implications since this description results in the avoidance of how these life assurance products are structured and the various layers of costs involved; because the discussion then focuses on the investment horizon and illustrative returns. More needs to be done to change the manner in which these products are marketed, perhaps resulting in a further TCF outcome; the reason being that whilst the products have a place within the financial planning environment they are not always suitable recommendations to the average client who is looking to invest funds for wealth creation or to save for a specific objective.

The categorisation of these products as life assurance policies means that, in addition to surrender fees and penalties, there are additional consequences to the restriction period applicable to, for instance, an endowment policy. In accordance with prevailing legislation the minimum restriction period applicable to an endowment policy is five years. During this five-year restriction period the insurance company may not allow an investor to either fully surrender the policy or to borrow the full investment value. Furthermore, in the event of the investor increasing the monthly or annual contributions by more than 20% of the previous year's contributions, a new five-year restriction period will be applied. This means that a 5-year term endowment policy could effectively become an 8- or 9-year term policy by one merely increasing one's premium in excess of what is allowed. These restrictions involved in investing in an endowment policy especially with regards to the liquidity and penalties are not adequately disclosed to potential clients to allow them to make an informed decision as to the policies' suitability to their needs and circumstances.

The failure therefore of FSPs to disclose the implications and consequences of terminating or transacting in endowment policies stems from the manner in which these policies are marketed and sold and that they are, in most instances, not appropriate to the client's needs and circumstances. These inappropriate recommendations and the resulting inability to make an informed decision by clients is the focus of the FAIS Ombud Office's investigations. In addition, one cannot ignore the levels of illiteracy in South Africa which makes it all the more necessary for financial services providers to do more than to expect that a signature on the documents means a financial services consumer understands the product. This must be considered against the level of detail involved in the products in question, some of which are not understood by the very financial services representatives who fail to provide appropriate 'Records of Advice' or indeed rely on generic 'Records of Advice' that do not indicate what was disclosed to the complainant or indeed why the recommended endowment policy is appropriate to the client's needs and circumstances.

Single Needs

There would appear to be a failure by Financial Services Providers ('FSP') and their representatives to appreciate the difference between providing the prospective client with a full financial needs analysis and compliance with the General Code of Conduct for Authorised Financial Services Providers and Representatives ('the Code'), specifically Section 8 (1) of the Code. The default response to complaints received by FSPs when questioned, with regards to the appropriateness of the product recommended, would appear to be that as the transaction represented a single need such as saving for retirement, applying for life cover etc., and that there was no need to conduct a full financial needs analysis, the information collected was not sufficient to provide appropriate advice and the client was advised as such. The Code as amended on 26 June 2020 provides in section 8 (1)(a): A provider [other than a direct marketer,] must, prior to providing a client with advice, obtain from the client such information regarding the client's needs and objectives, a financial situation risk profile and financial product knowledge and experience as is necessary for the provider to provide the client with appropriate advice.

Prior to the amendment on 26 June 2020 section 8 (1)(a) of the Code required that an FSP must, prior to providing a client with advice, take reasonable steps to seek from the client appropriate and available information regarding the client's financial situation, financial product experience and objectives to enable the provider to provide the client with appropriate advice. Therefore, even if a transaction would appear to relate to what is termed a single need, the FSP is still required to gather information specific to that need to ensure that appropriate advice can be provided. It cannot be accepted that a prospective client for example who has retired and is looking to obtain advice with regards the most appropriate options to invest his pension proceeds, a decision that has finite and lasting implications, is not provided with advice that considers his financial situation, needs and circumstances because the transaction represents a single need and a full financial needs analysis was not conducted.

Records of Advice

There is a growing trend towards standard generic advice records that not only provide generic statements such as “I can confirm that all fees and charges were disclosed to me.” Or “I can confirm that all material terms and conditions of the policy were explained to me and that I was able to make an informed decision” but these records also, more often than not, require the client to merely tick a box next to these generic statements. The concern surrounding these records of advice is that whilst the complainant has signed or ticked in confirmation of the fact that aspects such as fees and charges were discussed or that material terms and conditions were disclosed, one cannot expect that the complainant would be able to confirm indeed what was disclosed with regards to fees and charges, for example what was comprehensive or indeed a correct representation that would have allowed the complainant to have made an informed decision. The Code requires that concise details be provided of the material terms of the contract to allow the client to make an informed decision. The word ‘material’ has been highlighted as an FSP is required to have knowledge of the client’s needs and circumstances and ought to be in a position to identify the terms and conditions, exclusions etc. that would be material to their specific client which would need to be disclosed. The requirement that an FSP maintain a record of the advice provided it is twofold in that it is first and foremost, as the name suggests, a mechanism to record the advice provided and the basis for the advice provided to demonstrate that the client was placed in a position to make an informed decision.

The record of advice is also a mechanism that, if used correctly, will stimulate discussion with regards to the important aspects of the financial planning process and ensure that the FSP indeed covers all aspects required to indeed assist the client in making an informed decision. These generic records of advice, which appear to have been drafted to assist FSPs to automatically comply with the various sections of the Code, do not assist in either of these two respects and in fact fall short of compliance with the Code and detract from the financial planning process. These generic documents, which are seen as cumbersome and additional administration, are often grudgingly and apologetically provided to the client for completion when finalising the application process which merely pays lip service to the provisions of the Code instead of utilising this process in the spirit for which it was intended to enhance the financial planning process and provide a more holistic service to the benefit of all parties involved in the transaction. The financial services industry needs to embrace the importance of advice records and better equip their representatives and financial planners through training initiatives to know their clients so that they are better placed to identify the material terms that need to be disclosed to a specific client.

> *“We cannot change what we are not aware of, but once we are aware, we cannot help but change.”*

Forex Investments

As reported on in the 2018/2019 Annual Report, there continues to be an increase in forex investment complaints. The current financial climate, even before the impact of COVID-19, has seen consumers of financial services lured by the attractive promises made of high returns and easy profits. The increased access by individuals to the various social media platforms has also contributed to this increase in forex investments as these entities, most of which are not registered with the Financial Services Conduct Authority (‘FSCA’) utilise these platforms to source prospective clients with promises of instant wealth. These often turn out to be scams and clients lose all their funds. Whilst the Office of the FAIS Ombud appreciates that the economic climate has placed a strain on many households there is no quick fix and the old adage that if it is too good to be true it probably is, has never more appropriate and consumers are advised to be wary of these products.

Forex investments do have a place within the financial planning environment and may provide a prospective client with the benefits of diversification within an investment portfolio. However, forex investments are very technical products that require in-depth understanding and should never be entered into without obtaining appropriate advice as to whether an investment of that nature is beneficial to one’s financial situation and circumstances.

Consumers also need to be aware of those entities that, in an attempt to circumvent the FAIS Act and its corresponding legislation, entice clients by offering forex training software with the promise of turning an ordinary individual into a forex trader. Subsequent to the conclusion of the transaction the client is then offered broker services by the entity which is then that losses are incurred that were not explained or substantiated.

Adv Nonku Tshombe
Ombud