Treating Customers Fairly:
A new name for existing principles?

by

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Abstract

The meander of the South African financial industry, and in particular the issue relating to the inadequate protection that is currently being afforded to financial customers, is gradually becoming a growing concern. It is against this background that this dissertation examines the Financial Services Board's "Treating Customers Fairly" (TCF) initiative as a regulatory approach that seeks to ensure that providers of financial products and services treat their customers fairly. This dissertation commends the regulator for actively contributing towards achieving a fair deal for consumers. The implications of embarking on a quest for fairness within the financial services industry is prone to result in financial stability and consumer confidence. However, this dissertation asks whether TCF has made the Financial Advisory and Intermediary Services Act 37 of 2002 (FAIS Act) redundant and whether TCF appropriately explains the meaning of 'fairness'. If the latter can be answered in the negative, then this dissertation argues that TCF will exist as a twee and trite regulation which will not only serve as a mere duplication of the FAIS Act but also as a value system which will inevitably amplify the confusion relating to 'fairness'. The overall intention of this dissertation is to argue in favour of a properly integrated regulatory framework within the financial services industry. Shortcomings cannot be overcome by implementing what is essentially a foreign set of principles. Rather, the FAIS Act should be evaluated in order to see whether the TCF principles are not already part of our legislative framework.

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Chapter 1: Introduction and problem statement

1. General

> The financial services sector touches the life of each and every South African. It enables economic growth, job creation, the building of vital infrastructure and sustainable development for South Africa and her people. It is, therefore, crucial that the sector is well-regulated and stable.
>
> - National Treasury policy document titled "A safer financial sector to serve South Africa better"[1]

It is unfortunate that the journey towards a well-regulated and stable sector is not a smooth one. Everyone – individuals and companies from all over the world – who transact through financial institutions often face certain types of abuse in the financial sector such as excessive fees and an array of incomprehensible charges, the design and sale of inappropriate products and reckless lending often coupled with outrageous (and illegal) debt-collection practices.[2] To add to these complexities, financial institutions are aware that most customers assent to contracts without understanding the laws that bind them and with that their rights and duties. Often, financial institutions end up conducting their businesses in ways that prejudice financial customers – all in the name of self-interest, greed and power.[3] This glut of outrageous malpractices in the financial industry is often exacerbated by inadequate regulation as well as the refusal by various stakeholders to abide by the underlying rules.

An example of a well-known aftermath that was caused by, more or less, a combination of these abovementioned complexities was the 2008 global financial crisis. This crisis scarred the world economy. South Africa was fortunate enough to not have suffered severe direct effects of the global financial crisis, mainly because of its very strong regulatory framework for the

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1 National Treasury "A safer financial sector to serve South Africa better" (23 February 2011) 1 http://www.treasury.gov.za/documents/national%20budget/2011/A%20safer%20financial%20sector%20to%20serve%20South%20Africa%20better.pdf (13-7-2015) (NT Policy Document).

2 National Treasury "Treating Customers Fairly in the financial sector: A draft market conduct policy framework for South Africa" (December 2014) 6 http://www.treasury.gov.za/public%20comments/FSR2014/Treating%20Customers%20Fairly%20in%20the%20Financial%20Sector%20Draft%20MCP%20Framework%20Amended%20Jan2015%20WithAp6.pdf (13-7-2015) (NT Discussion Document).

3 NT Discussion Document (n 2) 6.

financial system, which is supported by strong regulatory institutions. Due to its prudent regulatory steps, it is justifiable to state that South Africa has been cushioned from the worst effects of this crisis.[4]

The upheaval that ensued in the global economy prompted many countries to re-evaluate their financial sector policy priorities. South Africa is one of the countries that jumped onto the same bandwagon of committing itself to a number of new, amended regulatory reforms in pursuit of creating a financial sector which is safer and better for all. The wide-ranging reforms that took place in South Africa target areas such as the insurance industry,[5] the retirement and pension funds industry,[6] the banking sector,[7] as well as the investment sector.[8] One of the most important strands of committing to a wide-range of reforms has been the effort to improve market conduct regulation. In the National Treasury's 2014 discussion document titled "Treating customers fairly in the financial sector: a draft market conduct policy framework for South Africa", much consideration was given to market conduct regulation mainly to address issues relating to consumer protection and the fair treatment of customers by financial institutions.[9] The discussion document affirmed that the Twin Peaks reform is an important opportunity to modernise South Africa's market conduct regulatory framework. It was held that a dedicated market conduct authority will underpin stronger and more effective customer protection for the financial services sector.[10]

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4 Lin, Edvinsson, Chef and Beding *National Intellectual Capital and the Financial Crisis in Israel, Jordan, South Africa, and Turkey* (2013) 54.

5 The FSB and the South African insurance industry have established a risk-based supervisory regime for the prudential regulation of both long-term and short-term insurers in South Africa – namely the Solvency Assessment and Management (SAM) project. FSB "Solvency Assessment and Management 2014 update" (April 2014) 5 https://www.fsb.co.za/Departments/insurance/Documents/SAM%202014%20update.pdf (13-9-2015) 5.

6 NT Policy Document (n 1) 18. Regulation 28 of the Pension Funds Act 53 of 1998 has been amended to allow banks access to more long-term financing: pension funds will now be allowed to buy long dated bank debt. In addition, there have been changes to the definition of "cash", which will reduce the incentives for pension funds to hold large amounts of short-term operational funds outside the banking system.

7 *Ibid* 9. The introduction of Basel III (an international standard) in South Africa's financial sector is envisioned to bolster the regulatory framework for banks.

8 *Ibid* 21. Proposals are being put in place to regulate private pools of capital, including hedge funds.

9 NT Discussion Document (n 2) 6.

10 *Ibid* 24.

2. A shift towards a Twin Peaks system of financial sector regulation

The Twin Peaks system has been dubbed "one of the most fashionable regulatory models" since the global financial crisis,[11] mainly because most countries decided to diverge from their initial consolidated regulatory structures in pursuit of strengthening their financial regulation through the separation of regulatory functions.[12]

South Africa already has a strong financial architecture which enabled it to be resilient throughout the financial crisis; however, the government cautioned against being complacent and proposed to move towards a "Twin Peaks" model of a financial regulation.[13] The Twin Peaks model is aimed at separating two regulatory functions. The one function will be governed by a prudential regulator, operating within the South African Reserve Bank (SARB), which will assume the responsibility of overseeing regulated financial institutions such as banks and insurers. The other function will be governed by a market conduct regulator that will be established by the Financial Services Board (FSB), which will be responsible for protecting consumers of financial services and promoting confidence in the South African financial system.[14]

Financial stability and consumer protection are two of the four policy objectives set out in the policy document titled "A safer financial sector to serve South Africa better". The Twin Peaks model is entrusted with the duty of ensuring that these objectives are achieved, whereby different regulatory authorities are given the lead responsibility to maintain and enhance the

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11 Mhango "Twin Peaks is not for SA" (6 February 2014) *News 24* http://m.news24.com/Fin24/Companies/Financial-Services/Twin-Peaks-is-not-for-SA-20140205 (15-7-2015).

12 In NT Policy Document (n 1) 28, the National Treasury expressed the view that after the financial crisis broke out in 2007, there was a global shift away from a single-regulator model towards a twin-peak model. Mhango argues in his article published in News24 (n 11), "Twin peaks is not for SA", that there is a substantial amount of exaggeration in the National Treasury's justification that there has been a global shift towards Twin Peaks. He contends that it is true that many countries across the globe have reformed their regulatory structures since the global financial crisis, however, it cannot be said that there has been a global shift towards twin peaks based on the fact that countries such as the United Kingdom, Canada, Australia and Netherlands have adopted the twin peaks model within their financial regulatory system.

13 Financial Regulatory Reform Steering Committee "Implementing a twin peaks model of financial regulation in South Africa" (1 February 2013) 6 http://www.treasury.gov.za/twinpeaks/20131211%20-%20Item%203%20Roadmap.pdf (15-7-2015) (FRRSC twin peaks model).

14 FRRSC twin peaks model (n 13) 6.

key policy objectives.[15] Since South Africa is facing a multiplicity of market abuses as well as shortfalls when it comes to consumer protection, it is presumed that the Twin Peaks approach will be the suitable option to provide optimal means of ensuring that transparency, market integrity, and consumer protection receive sufficient priority.[16]

3. Adopting the Treating Customers Fairly framework

The FSB, the recently proclaimed market conduct regulator, has been in constant engagement with the industry to mitigate perilous instances of consumers being exploited by financial institutions. To tackle this challenge, the FSB decided to borrow liberally from English law by copying a well-known comprehensive global initiative entitled Treating Customers Fairly (TCF) as a contribution towards stricter market conduct oversight.[17] TCF was founded by the United Kingdom (UK) with the intention of fulfilling its regulatory objectives stipulated under the Financial Services and Markets Act of 2000 (FSMA).[18] The Financial Services Authority (FSA), as the independent body, assumed the supervisory duty of overseeing the operation of TCF, as well as the greater financial services industry in the UK.

TCF is a principles-based approach which seeks to ensure that the fair treatment of customers is embedded within the culture of financial firms.[19] It is held that the potential benefits of using principles is that they provide flexibility, they are more likely to produce behaviour which fulfils the regulatory objectives, and are easier to comply with.[20] The FSA in the UK shared the same sentiments when they initially implemented TCF as part of their

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15 FRRSC twin peaks model (n 13) 7.

16 NT Policy Document (n 1) 29. See also Dincer and Hacioglu *Globalization of Financial Institutions: A Competitive Approach to Finance and Banking* (2014) 190.

17 Financial Services Board "Treating Customers Fairly: The Roadmap" (2011) 6 https://www.fsb.co.za/feedback/Documents/Treating%20Customers%20Fairly%20-%20The%20Roadmap%202011.pdf (10-7-2015) (FSB TCF roadmap).

18 These regulatory objectives are mentioned under part 1 of the FSMA. The regulatory objectives are market confidence, financial stability, public awareness, the protection of consumers and the reduction of financial crime.

19 FSB TCF roadmap (n 17).

20 Black, Hopper, Band and Smith "Making a success of principles-based regulation" 2007 *Law and Financial Markets Review* 193.

regulatory framework. According to the FSA, principles are simplified rules which are less prescriptive, less intrusive and promote clear communication.[21]

The TCF approach suggests a shift towards a culture of flexibility and adaptability by requiring firms to actively work out, at their own accord, what practices constitute fair treatment to customers. Firms are required to monitor and measure for themselves whether they are treating customers fairly and have embedded TCF in their organisational culture. Self-regulation allows firms to enjoy a considerable degree of freedom to make sense of TCF and to translate it into everyday business practice.[22]

According to TCF, firms are strongly encouraged to consider these six fairness outcomes when implementing their TCF initiatives and in assessing whether the changes they are implementing are having an impact on their ultimate objective of treating customers fairly.[23] These outcomes are as follow:

- Outcome 1: Customers are confident that they are dealing with firms where the fair treatment of customers is central to the firm culture.

- Outcome 2: Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.

- Outcome 3: Customers are given clear information and are kept appropriately informed before, during and after the point of sale.

- Outcome 4: Where consumers receive advice, the advice is suitable and it takes account of their circumstances.

- Outcome 5: Consumers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and what they have been led to expect.

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[21] Financial Services Authority "Treating customers fairly – towards fair outcomes for consumers" 2006 http://www.fca.org.uk/static/fca/documents/fsa-tcf-towards.pdf 5, 24, 42 (10-7-2015) (FSA TCF).

[22] Georgosouli "The FSA's 'treating customers fairly' (TCF) initiative: What is so good about it and why it may not work" 2011 *Journal of Law and Society* 417.

[23] FSB TCF roadmap (n 17) 7.

- Outcome 6: Customers do not face unreasonable post-sale barriers to change product, switch provider, submit a claim or make a complaint.

The TCF initiative is relevant to all firms who provide retail financial services, whether they have a direct interface with the customer or not and whether or not they are involved in all stages of the product life-cycle.[24] This includes product suppliers and financial services providers. Refer below to figure 1 for a basic illustration of a typical product life-cycle. [25]

Figure 1:

The TCF Product Life-cycle

4. Current positioning of the FAIS Act

Despite the FSB introducing TCF as part of South Africa's market conduct regulation, it is worth affirming that the FAIS Act is still presently in force and it should be complied with. For the past decade, its momentum has brought about drastic implications for financial advisors and intermediaries.[26] The statute is intended to oversee "the control in terms of the Act of any activities relating to financial services rendered by financial institutions, and to advise the Minister of Finance on matters concerning such financial institutions".[27] Furthermore, the FAIS Act imposes the duty on advisers and intermediaries to adhere to the General Code of Conduct (GCC) which sets out minimum standards for conduct towards the consumer.

[24] FSA TCF (n 21) 9.

[25] FSB TCF roadmap (n 17) 8.

[26] Hattingh and Millard *The FAIS Act Explained* (2010) 2.

[27] Millard and Botha "Something's got to give: The future of financial advisors and intermediaries as employees" 2012 *THRHR* 44.

The FSB is tasked with supervising the FAIS Act and financial services which are governed by the FAIS Act.[28] Unlike other financial services, the credit industry falls outside the scope of the FSB and the FAIS Act. The credit industry is regulated by the National Credit Regulator (NCR) who has been assigned the primary responsibility to regulate persons that provide credit (credit provider) under the National Credit Act 34 of 2005 (NCA). However, in some instances the FAIS Act will also be applicable where for example the credit provider requires a customer to take out insurance for an asset that the credit provider is financing and the credit provider facilitates the conclusion of the insurance transaction.[29] In this instance, the FAIS Act will regulate the insurance transaction considering the fact that insurances fall under the FAIS Act's mandate.

The FAIS Act contains measures on the protection of financial-services consumers from unscrupulous and unfit financial institutions. In fulfilling these measures, the FAIS Ombud is mandated by the FAIS Act to adjudicate on particular matters concerned with the mis-selling of financial products and misleading advice.[30] The existence of the FAIS Ombud is justified by the need to provide financial customers with an expedient, inexpensive and effective ombud scheme as an alternative to approaching civil courts in order to enforce their rights.[31] Section 20(3) of the FAIS Act expressly stipulates that "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 the circumstances". In light of section 20(3) of the FAIS Act, it is important to consider section 34 of the Constitution,[32] which provides that—

[28] The FSB was established by the provisions of the Financial Services Board Act 97 of 1990. Millard and Botha (n 27) 44 state that "[c]urrently, the FSB controls the following Acts, namely, the Collective Investment Schemes Control Act 45 of 2002 (CISCA); the Financial Services Board Act 97 of 1990 (FSB Act); Financial Institutions (Protection of Funds) Act 28 of 2001 (FI Act); Financial Supervision of the Road Accident Fund Act 8 of 1993 (FSRAF Act); Friendly Societies Act 25 of 1956 (FS Act); Inspection of Financial Institutions Act 80 of 80 of 1998 (IFI Act); Long-term Insurance Act 52 of 1998 (LTIA); Pension Funds Act 53 of 1998 (PFA); Short-term Insurance Act 53 of 1998 (STIA); Supervision of the Financial Institutions Rationalisation Act 32 of 1996 (SFIR Act); Securities Services Act 36 of 2004 (SSA); and, of course, the FAIS Act."

[29] The scope of this dissertation will only consider the terms "financial products", "financial services" and "financial services provider" as defined in section 1 of the FAIS Act and as regulated by the FSB.

[30] Millard "Bespoke justice? On financial ombudmen, rules and principles"2011 *De Jure* 236.

[31] *Ibid* 232.

[32] Constitution of the Republic of South Africa, 1996.

> [e]veryone has the right to have any dispute that can be resolved by the application of law decided in a fair public hearing before a court or, where appropriate, another independent and impartial tribunal or forum.

As far as reasonable and equitable interpretation is concerned, it should be noted that section 34 of the Constitution calls for matters to be heard by a court "or, where appropriate, another independent and impartial tribunal or forum". This would clearly include the Ombud.[33] As a result, one can safely conclude that section 20(3) of the FAIS Act is in line with section 34 of the Constitution. Not only does it provide a complainant with a competent forum for settling of a dispute but it also provides for a fair public hearing.[34]

The FAIS Ombud's Annual Report, which was published late last year, reported that the Ombud encountered an increase in complaints during the 2013/2014 financial year – the issues primarily dealt with intermediaries selling investment products.[35] The Minister of Finance, Mr Nene, firmly held the view that the high number of complaints indicates that the FAIS Ombud is fulfilling a crucial role as one of the key avenues that seek to address the need for redress.[36] Rattue, on the other hand, addresses the issue relating to the increase in complaints in a different light. He is of the view that the ongoing increase does not only comprise of the malfeasance on the part of advisers; he asserts that it is also due to consumers becoming more aware of their rights since the advent of the FAIS Act.[37] For instance, consumers are aware that financial providers have a general duty to "to render financial services honestly, fairly, with due skill, care and diligence, and in the interests of clients and the integrity of the financial services industry".[38] Should a customer allege that the financial provider rendered financial services which lacked the prescribed minimum standard imposed by the GCC, the consumer has every right to approach the FAIS Ombud for redress. In spite of the increase in the number of

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33 Millard (n 30) 175.

34 Millard (n 30) 175-176.

35 FAIS Ombud Annual Report 2013/2014 http://www.faisombud.co.za/sites/default/files/publications/AR%202013-2014.pdf (4-10-2015).

36 Minister's report published in the FAIS ombud annual financial report during financial year 2013/2014 http://www.faisombud.co.za/sites/default/files/publications/AR%202013-2014.pdf (4-10-2015).

37 Rattue "Has TCF made the FAIS act superfluous?" 2015 *Money Marketing* 10.

38 Section 2 of the GCC.

complaints, it is worth recognising that the Ombud has continuously strived to achieve their strategic goal of resolving complaints, which is highly commendable.

5. TCF and the FAIS Act obligations

For many years, the concept of fairness has been omnipresent in South Africa's financial regulatory environment. The fact that the FAIS Act has been in existence for over ten years makes it evident that the FSB – together with the FAIS Ombud – has maintained an uncompromising stance against any unfair treatment towards consumers. So what is different about the FSB's new venture of introducing a "more principles-based approach" in the form of TCF? Does the shift towards broadly stated principles rather than more detailed rules suggest that the FSB's market conduct objectives will be effectively achieved? Millard states that "regardless of one's sentiments, the fact remains that financial law is complicated and that despite the best attempts of the legislator, all these rules still leave role players in the financial sphere discontented".[39] Emphasis should not be placed entirely on the language of the stipulation but more on what it requires and, most importantly, one should note that a good set of rules should ultimately support a principle.[40] Whether or not the regulator agrees with Millard's affirmation is debatable. However, this dissertation is inclined to support this view.[41]

6. The structure of the dissertation

The greater focus of this dissertation is concerned with the efforts taken to ensure customers are treated fairly in the context of market conduct regulation. There are numerous key advantages of TCF. One undeniable advantage is its ability to address the issue of consumer protection at all stages of the firms relationship with the customer, from the product life cycle to the organisational structures and processes. However, this dissertation intends to demonstrate that TCF does not make the meaning of "fairness" any clearer. In fact, the Financial Sector Regulation Bill (FSR)[42] which is set on introducing the six broad outcomes, in

[39] Millard (n 30) 234.

[40] *Ibid* 235.

[41] See Chapter 4 of this dissertation for more information regarding this view.

[42] The first draft of the Financial Sector Regulation Bill was published in December 2013. The revised draft of the Bill was published 10 December 2014.

addition to the existing laws, is bound to create more confusion. Furthermore, this dissertation sets out to illustrate that the six TCF outcomes are actually already aligned with the rules provided for in the FAIS Act. Each outcome can be construed to be indirectly embedded within the FAIS Act. The dissertation will therefore discuss each TCF outcome individually by juxtaposing them to the actual, existing FAIS Act obligations. It will also critically examine why the implementation of the TCF initiative will likely produce inadequate results in South Africa due to the uncertainties regarding what fairness really means and whether the quest towards understanding fairness is getting any clearer. Finally, the need for a proper legislative framework, which embodies fairness in specifically defined rules, will be proposed as a way forward in addressing abusive market conduct.

Chapter 2: Treating Customers Fairly and the FAIS Act

Introduction

It is accepted that the FSB steered the TCF initiative to signal a shift from a heavily rule-based approach to a more principles-based approach. The six fairness outcomes resonate with TCF's overall goal of ensuring that all firms treat their customers fairly at all levels of their organisation and throughout their product life-cycle. However, the nature of TCF seems to be aligned with the FAIS Act, which already imposes extensive obligations on authorised financial services providers and their representatives. In addition to that, the FAIS Ombud adjudicates numerous cases which highlight the fact that fairness outcomes are already central to the FAIS Act.

1. Outcome 1: Consumers are confident that they are dealing with firms where the fair treatment of customers is central to the firm's culture

According to the FSB, if financial advisors make it their primary responsibility to fully embed the first outcome within the firm's culture, the delivery of the remaining five outcomes should follow as a matter of course.[43] In order to get fully embedded in the culture, financial advisors will need to give great consideration and commitment to the ideology of Treating Customers Fairly throughout the stages of the product life-cycle to which they contribute, from product design and marketing, through to the advice, point-of-sale and after-sale stages.[44] Firms will also be required to demonstrate the incorporation of the TCF approach at all levels of planning, decision-making, management and operations within the firm.[45] Since TCF is a self-regulatory initiative, the board and senior management[46] of a financial firm are required to monitor and

[43] FSB TCF roadmap (n 17) 20.

[44] *Ibid* 7.

[45] *Ibid* 20.

[46] Georgosouli (n 22) 412 referred to H Sants' "The FSA retail agenda: Working with the industry" speech at the FSA AIFA Dinner, 21 November 2007, where it was elaborated that senior managers are thought to be in a better position to know how their internal processes need to be structured in order to bring about TCF outcomes.

measure the success rate of their own performance in treating customers fairly and embedding TCF principles in their organisational culture.[47]

1.1. TCF outcome 1 aligned with the existing FAIS Act obligations

Although the obligations in terms of the FAIS Act are largely compliance and rules based, there are sections which support certain principles and actually underpin the first TCF outcome. For example, section 16(1)(a) of the FAIS Act prescribes that a provider "must at all times render financial services honestly, fairly, with due skill, care and diligence, and in the interest of clients and the integrity of the financial services industry". Moreover, section 16(1)(b) states that financial services providers "must act with circumspection and treat clients fairly in a situation of conflicting interests". Section 2 of the General Code of Conduct (GCC) goes on to reiterate exactly what is stipulated in section 16(1)(a).

It is significant to draw specific attention to the legislature's express usage of the words "must *at all time*", which are contained in section 16 of the FAIS Act and section 2 of the GCC. For the sake of sensibleness, these words can be interpreted to mean that the legislature expects demonstrable commitment from senior management within financial institutions to *always* treat customers fairly. The FAIS Ombud will most likely find a financial institution's level of compliance wanting if it fails to demonstrate that indeed it acted honestly and fairly, and with due skill, care and diligence, in the interests of the consumer and the integrity of the financial industry. It is only through the application of these precepts that one can cultivate a culture of confidence in consumers. Financial institutions should not fall foul of acting in accordance with these general provisions of the FAIS Act, they should always act with circumspection when considering the clients' interests and should be able to demonstrate that the fair treatment of customers is central to the firm's organisational structures and processes. This statement is supported by the interpretation that was given to section 16(1)(a) and (b) by the FAIS Ombud and the next paragraph discusses this aspect.

[47] FSB TCF roadmap (n 17) 21.

1.2. FAIS Ombud case studies

1.2.1. *J Kearney v AR Strauss Financial Services (Pty) Ltd*[48]

In this case, the complainant took out a combined short-term insurance policy through the respondent's representative (Renasa). The insurance was administered by a company called Dex and underwritten by Renasa. Renasa undertook to stop doing business with the respondent, due to the size of premium received from it. This meant that Renasa would cease to offer cover to all short-term insurance policyholders under the respondent's portfolio and all policyholders who enjoyed short-term insurance cover from Renasa would be left without cover unless the respondent took steps to remedy the situation.[49] The respondent decided to take a remedial step by transferring its short-term insurance book to another broker, who would ensure that the affected policyholders enjoyed cover from another short-term insurer.[50] For some reason, the complainant's record with the respondent was never transferred to the new broker.[51] Subsequently, the complainant's house was burgled whereby furniture, jewellery, clothing and equipment, which would have been covered by the policy underwritten by Renasa, were stolen.[52] The complainant informed the respondent and the respondent advised the complainant that there was no insurance cover in place as the existing insurance policy had been cancelled. The complainant alleged that neither she nor her husband was responsible for cancelling the policy.[53]

As a result of the investigation by the Ombud, it was established that it was not the complainant's fault but it was as a result of the respondent's failure notify the complainant that she will no longer have cover under Renasa and to ensure that the complainant's account was transferred to the new broker. One of the issues considered by the Ombud was whether the respondent complied with section 2 of the GCC, which states that providers "must at all times render financial services honestly, fairly, with due skill, care and diligence, and in the interest of clients and the integrity of the financial services industry". The Ombud stated that at the time

[48] FOC 1663/05 GP, issued 13 November 2006.
[49] Par 3.
[50] Par 4.
[51] Par 5.
[52] Par 6.
[53] Par 9.

the respondent decided to transfer its books to another broker, it failed to ensure that the complainant's records were also successfully transferred.[54] The notions of care and diligence required the respondent to follow up on all communication with all its short-term insurance clients to ensure that none of its clients were left out. The Ombud ruled that the respondent failed to act in accordance with the requirement under section 16 of the FAIS Act, read with section 2 of the GCC.

1.2.2. *JA Steenkamp v Old Mutual Life Assurance Company SA Ltd*[55]

In this particular case, the complainant requested the representative of the respondent to authorise a claim for medical expenses as his son had been hospitalised. Authorisation was granted by the respondent, but further authorisation was sought by the complainant to administer a drug for the treatment of a lung infection.[56] The respondent investigated reasons for the medication and found that the complainant's son had certain medical conditions which they alleged were not disclosed to them.[57] The representative rejected the claim for medical expenses and subsequently cancelled the complainant's membership to the respondent's medical aid scheme as a result of the alleged non-disclosure of material information by the complainant.[58] Central to this particular dispute was the question whether the respondent's argument of material non-disclosure has merit. The FAIS Ombud took into consideration that the complainant is a construction worker with standard 8 as the highest standard passed and he also attended a special school which assists learners who are academically weaker in developing their technical skills. The Ombud opined that it was the broker's duty to assist the insured in disclosing material information: this flowed from the representative's duty to have

[54] Par 16.3.
[55] FOC 1343/05 FS, issued 13 March 2006.
[56] Par 11 and 12.
[57] Par 13.
[58] Par 14.

rendered the financial service with due skill, care and diligence, which, if had he done, the complainant would not have suffered financial loss.[59]

2. Outcome 2: Products and services marketed and sold in the retail market should be designed to meet the needs of identified customers

This outcome vests on two stakeholders, the product supplier and the intermediary. The product supplier is bestowed with the responsibility of conducting various assessments in order to ensure that a product is appropriately designed for the needs of a particular target market. Conversely, when the intermediary provides advice on the product directly to the client, he or she should ensure that the product is appropriately allocated to the particular client concerned.[60] The intermediary would have to consider the consumer's needs, assess whether the client understands the risks associated with a particular financial product, and whether the client can afford to buy or invest in the financial product. Intermediaries will be expected to liaise directly with the product suppliers to obtain information that will assist them in determining for which particular client groups the product or service would be appropriate.

According to the FSB, TCF does not allow intermediaries to sidestep any responsibility for recommending an inappropriately structured product to a customer on the basis that it is the product provider's responsibility to design appropriate products. Intermediaries are expected to produce an appropriate level of product due diligence.[61] The same principle applies to product providers. Product providers need to ensure that intermediaries recommend products

[59] Par 25. Other FAIS Ombud cases that dealt with section 2 of the GCC include *Gary le Vatte v Rosspen Financial Services* FOC/600/05 EC, issued 29 September 2005 and *Johan Adriaan Steenkamp v Old Mutual Life Assurance Company (South Africa) Limited* FOC 1343/05 FS, issued 13 March 2006.

[60] According to the FSB TCF Roadmap (n 17) 15, the FSB expressly stated that a useful distinction can be drawn between ensuring the product is appropriate for a particular target market, and ensuring the product is suitable for the particular customer concerned. The former is mainly the product supplier's responsibility, and the latter is mainly the intermediary's responsibility.

[61] FSB TCF Roadmap (n 17) 15. In the case of *Ethel Ellouise Blessie and others v Shevgem Investments CC t/a Randsure Brokers & Jamey Randall* 02202/09-10/KZN/1, issued 25 January 2012, the Ombud stated that due diligence simply means that the financial services provider examines the company and the product it sells beyond the company-produced marketing material. Thus, among other basic things required when conducting due diligence, the financial services provider checks the legitimacy of the company to see whether it is properly registered and licensed by the authorities, establishes its history, examines the structure of that company to see whether it adequately affords protection its investors, looks into its directors, examines the viability of the product sold, and determines if its compatible with the needs of the investor.

that will meet the needs of the identified customers. Financial services providers must be able to also account for those products which they think will meet the needs of identified customers and be able to gauge the impact a product will have on a customer.

2.1. TCF Outcome 2 aligned with existing FAIS obligations

In many respects, the FAIS Act articulates the same principles. One of the purposes of drafting the FAIS GCC was to ensure that the client's reasonable financial needs regarding financial products will be appropriately and suitably satisfied. Section 8(1) of the GCC goes a step further by providing guidance on how a product adviser can achieve that desired purpose. It states that:

> [A] provider other than a direct marketer, must, prior to providing a client with advice—
>
> (a) 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;
>
> (b) conduct an analysis, for purposes of the advice, based on the information obtained;
>
> (c) identify the financial product or products that will be appropriate to the client's risk profile and financial needs, subject to the limitations imposed on the provider under the Act or any contractual arrangement.

If a financial provider alleges compliance with section 8 or any provision of the GCC, he or she must be able to produce a record of communication to support such an allegation. Section 9 of the GCC requires a provider to keep record of the advice that was furnished to the client. The record must reflect the basis on which the advice was founded (this includes a brief summary of the information and material on which the advice was based);[62] the financial products which were considered;[63] and the financial product or products recommended with an explanation of

[62] Subsection (a).

[63] Subsection (b).

why the product or products selected is or are likely to satisfy the client's identified needs and objectives.[64]

The below case illustrates the FAIS Ombud's stance against non-compliance with the duty of conducting a financial needs analysis before making any recommendations.

2.2. FAIS Ombud case study

2.2.1. *Margaret Lilian Posgate v D Risk Insurance Consultants cc and Deeb Raymond Risk*[65]

In this case, Margaret (the complainant) alleged that the respondent advised her to invest a hefty amount in public property syndication.[66] The investment was meant to provide a monthly income to the complainant as a means of maintaining her daily standard of living. Two years later, the monthly income payments had ceased.[67] Due to the financial prejudice that the complainant suffered, she requested the respondent to provide her with proof that he had conducted a needs analysis, a copy of the record of advice and her risk assessment.[68] She later learnt, subsequent to having discussions with another broker, that certain processes should have been followed when the respondent had sold the investment to her. The complainant sought relief from the Office of the FAIS Ombud.

The Ombud considered the issue of whether the respondent complied with the GCC in rendering financial services. If the respondent had conducted an analysis based on the information obtained from the client as envisaged in section 8 of the GCC, he would have been able to appropriately shortlist suitable financial products that fit the complainant's financial needs.[69] He would have also been able to identify and recommend a financial product that is

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64 Subsection (c).

65 FAIS 09479/10-11/GP1, issued 22 November 2012.

66 Par 4.

67 Par 5.

68 Par 7.

69 In *Jennifer Patricia Malan v Standard Bank Financial Consultancy – a division of Standard Bank Ltd case* number FOC 934/05/GP (1) issued 20 October 2005, the Ombud referred to the court per Kroon J in *Poultney v Absa Brokers and Another Eastern Cape Division* case number 430/200 (unreported) where it was stated at par 45 that "[a] needs analysis embraces not only a thorough analysis of the client's applicable affairs and actual financial needs, but also a determination, by the application of the adviser's knowledge and skills, of which services would best fulfil the client's particular needs (ILPA code, par.2.2). To be read therewith are the

commensurate to the clients risk tolerance and financial needs.[70] Furthermore, the respondent failed to maintain an appropriate and adequate record of advice, as required by section 9 of the GCC, as evidence that he conducted the required financial needs analysis. The Ombud ruled in favour of the complainant.

This case illustrates that there is already an obligation on financial services providers to gather as much information as possible to make sure that the designed products and services are appropriately sold to the intended market. The FAIS Ombud has often stressed the importance of adhering to this provision in order to minimise the risk of financial services providers recommending products which do not meet the needs of the customer.

3. Outcome 3: Customers are given clear information and are kept appropriately informed before, during and after the time of contracting

Financial providers always occupy a more favourable position compared to consumers when it comes to dealing with financial products or services. More often than not, consumers are not equipped with the relevant expertise to fully comprehend the nature of financial products. Given the unequal bargaining position between clients and financial advisers, clients should always be placed in a better position to protect their own interest.

The FSA explains the essence of the third outcome by stating that—

> [b]efore and at the point of sale, financial providers are expected to give customers information which is clear, fair and not misleading. Effective point of sale disclosure is also essential to enable customers to understand the characteristics of the product they are buying and to help them understand whether and why it meets their requirements. Post-sale disclosure plays an important role in helping to ensure that consumers are kept aware of product performance, their opportunities to act at certain points in the product lifecycle and changes in the terms and conditions.[71]

3.1. TCF outcome 3 aligned with existing FAIS Act obligations

To a large extent, the FAIS GCC has in-depth provisions dealing with the delivery of clear and appropriate information in order to promote openness, transparency and fairness. Reference

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provisions of para 2.9 of the code which required, inter alia, that the advantages and limitations of any service offered to a client should be explained to him or her so that an informed decision there anent might be made."

[70] Par 62.

[71] FSA TCF (n 21) 12.

will be made to certain sections relating to disclosure, however, one should note that the GCC contains a large amount of provisions that financial providers should adhere to.

Section 3 of the GCC requires financial providers to render information which is factually correct,[72] and the information must be provided in plain language, avoid uncertainty or confusion and must not be misleading.[73] Furthermore, the information must be adequate and appropriate in the circumstances of the particular financial service, taking into account the factually established or reasonably assumed level of knowledge of the client.[74]

The information provided to the client must be provided timeously so as to afford the client reasonably sufficient time to make an informed decision about the proposed transaction.[75] The financial provider should not omit disclosure of all relevant remuneration or monetary obligations payable to the product supplier or the provider.[76]

A financial provider should also provide a reasonable and appropriate general explanation of the nature and material terms of the relevant contract or transaction to a client, and generally make full and frank disclosure of any information that would reasonably be expected to enable the client to make an informed decision.[77] The provider must furthermore take reasonable steps to ensure that the client understands the advice and that the client is in a position to make an informed decision.[78]

The financial provider is required to disclose to the client the existence of any personal interest in the relevant service, or of any circumstance which gives rise to an actual or potential conflict of interest in relation to such service, and take all reasonable steps to ensure fair treatment of the client.[79]

[72] Section 3(1)(a)(i) of the GCC.
[73] Section 3(1)(a)(ii) of the GCC.
[74] Section 3(1)(a)(iii) of the GCC.
[75] Section 3(1)(a)(iv) of the GCC.
[76] Section 3(1)(a)(vii) of the GCC.
[77] Section 7(1)(a) of the GCC.
[78] Section 8(2) of the GCC.
[79] Section 3(b) of the GCC.

The financial provider should also implement appropriate procedures and systems that ensure that any verbal or written communication is recorded appropriately and that it is retrievable and safe from destruction.[80]

Under sections 4 and 5 of the GCC, a financial provider is required, at the earliest reasonable opportunity and only where appropriate, to furnish the client with full particulars relating to the relevant product supplier as well as full particulars relating to it as a financial provider.

After transacting, financial providers should have regular, ongoing contact with existing clients to provide them with key information relating to financial products at appropriate times. In making contact arrangements, section 6 of the GCC stipulates that a financial provider must, in all communications and dealings with a client, act honourably, professionally and with due regard to the convenience of the client. Financial providers should ensure they have up-to-date contact details of clients, and that the clients are in possession of the provider's correct contact details.

3.2. FAIS Ombud case study

3.2.1. *Stephanie Neethling v Vaidro 173 CC t/a Vaidro Investments and Andrea Moolman*[81]

In casu, the complainant alleged that she and her husband were having difficulty in keeping up with monthly payments on their endowment and life policies and subsequently invested a substantial amount of money in the Relative Value Arbitrage Fund (RVAF) based on the recommendation made by the respondent.[82] Following the demise of the RVAF, the complainant sustained a substantial loss. The complainant lodged a complaint with the FAIS Ombud based on the premise that the respondent failed to properly advise her in terms of the FAIS Act and the GCC. The complainant claims that she would not have entered into the transaction with RVAF had the respondent conducted herself in the manner expected of providers when they render financial services to clients – which was to disclose the real risk inherent in RVAF.

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[80] Section 2(a)(i)-(iii) of the GCC.

[81] FAIS 04269/12-13/ WC 1, issued 16 March 2015.

[82] Par 4.

The FAIS Ombud dealt extensively with the failure on the part of the respondent to appropriately disclose risks and carry out the necessary due diligence. Furthermore, the FAIS Ombud dealt comprehensively with key issues relating to disclosure under the FAIS Act and the GCC. The Ombud stated that the respondent did not take reasonable steps to ensure that the complainant understood "any material investment or other risks associated with the product".[83] If the respondent had given advice in plain language, the complainant would have been able to make an informed decision as required by section 8(2).[84] The Ombud also highlighted the failure by the respondent in providing reasonable and appropriate explanation of the nature and material terms of the transaction, and making full and frank disclosure of any information that would reasonably be expected to enable the complainant to make an informed decision.[85] At the very least, the complainant needed to know that she was investing in an unregulated entity.[86] In addition, she should have been told that she was dealing with a partnership where she would become a partner in *commandite* and the respondent should have explained the legal implications of such a partnership.[87] Furthermore, she should have been told that she stood the risk of losing her capital as there was no regulatory body to which RVAF was accounting to.[88] Finally, there should have been a disclosure to the effect that there were no financials, fund fact sheets or even a license number on any of the documentation.[89] The Ombud was convinced that the complainant would not have invested in RVAF had she been given the correct material information.[90] Finally, the Ombud found that the respondent failed to disclose fees in the manner prescribed by section 3(1)(vii) of the GCC. In particular, the amount was not reflected in specific monetary terms.[91] The Ombud upheld the complaint.

[83] Par 33.
[84] Par 34.
[85] *Ibid*.
[86] Par 35.1.
[87] Par 35.2.
[88] Par 35.3.
[89] Par 35.4.
[90] Par 36.
[91] Par 42.

This case shows that the FAIS Act provides extensively for disclosures. Failure to properly disclose is not only unlawful but is also potently unfair. Therefore it can be said that there is ample evidence that this particular TCF outcome is already incorporated in the FAIS Act.

4. Outcome 4: Where customers receive advice, the advice is suitable and takes into account the customers circumstances

It is unfortunate that in some instances financial services providers will mis-sell products all in the name of self-interest and greed. The TCF initiative cautions these stakeholders against any malfeasance in providing inappropriate advice.

This outcome requires firms to provide good quality advice to customers.[92] In order to do that, firms need to obtain significant information from customers to be able to test the suitability of the product. They also need to adequately explain the risks and implications of a particular course of action before transacting with the customer. These are some of the most important procedures firms should follow so that they can avoid mis-selling and causing actual consumer detriment.[93] The same principles apply when recommendations are made to consumers. The recommendations must reflect the customer's needs, priorities and circumstances.[94]

There is some overlap between this outcome and the two previous outcomes – outcome 2 and outcome 3. Outcome 2 already requires financial services providers to take into the account the needs of the customer which inevitably means that the customer's circumstance should also be taken into account. Outcome 3 regulates the manner in which advice is given and the necessity to disclose risks and implications of a particular product or service, and failure to adhere to this outcome will inevitably result in unsuitable advice. Therefore, what is

[92] In the UK, the requirement on firms to deliver suitable advice is not a new concept – it is firmly rooted in their Principles for Business. In particular, Principle 9 which states that "a firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgement".

[93] FSA TCF (n 21) 36. The FSA has a TCF cluster which was aimed at putting systems and advice generating processes in place in firms providing advice on mainstream investment products. The objective was to help firms improve their advice processes and reduce the risk of mis-selling. The findings are most relevant to firms operating in the retail investment advisory market, but the work also looked at small numbers of product provider firms with direct sales forces and retail banks offering investment advice.

[94] FSA TCF (n 21) 12.

discussed in outcome 2 and 3 above also applies to this outcome. Having said this, the next paragraph provides a more specific analysis without causing any further confusion.

4.1. TCF outcome 4 aligned with existing FAIS Act obligations

Section 8 of the GCC specifically makes provision for providers to give suitable advice. It reiterates the abovementioned views that financial providers need to obtain appropriate information from the customer and conduct an analysis based on the information obtained in order to provide the customer with suitable advice. As part of the advice-giving process, it is advisable for the financial provider to be upfront with the customer about the existence of any personal interest or potential conflict of interest.[95] Such disclosure will allow the financial provider to give advice which is not tainted with unscrupulous intent. The financial services provider must take all reasonable steps to ensure fair treatment of the client by providing suitable advice regardless of the specific incentive or remuneration he or she may be receiving from a product provider, intermediary or any third party.

Another important provision that complements the advice-giving process is the need to keep record of advice that has been given or feedback which has been received from customers.[96] Financial providers will have to monitor the records which have been kept so that they can identify any inconsistencies, irregularities or inappropriateness. The UK's Cluster Report[97] indicates that approximately half the firms which have been reviewed did not monitor their quality of advice. It was also common for firms that obtained some form of management information not to act on it. It is to be expected of senior management to have systems in place to satisfy themselves that fair treatment of customers is being delivered throughout the firm.[98]

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95 Section 1 (b).

96 Section 9 FAIS Act.

97 See FSA "Quality of advice cluster report" (July 2006) http://www.fsa.gov.uk/pages/doing/regulated/tcf/library/cluster/advice/index.shtml (21-09-2015). The reports include the results of firms that have been reviewed by the FSA. The purpose of the review is to evaluate systems and controls that firms implement in order to embrace a TCF culture within their businesses. The results are intended to provide guidance for firms and others considering the implications of TCF in specific circumstances. And they also provide some practical examples of good and bad practice for firms to consider in their implementation of TCF.

98 FSA TCF (n 21) 37.

The quality of advice is reliant on the quality of financial providers. According to the UK's Cluster Report, it was found that the quality of advice was much better in firms which had a robust training and competence regime. Approximately one-third of firms sampled did not have adequate training and competence procedures in place.[99] Firms need to ensure that adequate training is in place in order for financial providers to be better positioned to provide adequate advice. Once financial providers are equipped with the right expertise, they will be able to assess whether a particular piece of advice would be fitting in the circumstances of the particular financial service, taking into account the factually established or reasonably assumed level of knowledge of the client. Therefore, a proper record-keeping process as required in section 9 of the GCC will be able to indicate any training needs which should be put in place.

4.2. FAIS Ombud case study

4.2.1. *Rukshana Ramdass vs Standard Bank financial consultancy – a division of Standard Bank Ltd*[100]

In casu, the complainant asserted that the representative advised her to purchase a financial product, Excelsior Endowment, without taking into account her needs and objectives.[101] The complainant further alleged that the representative did not disclose the true nature of the product to her. The complainant sought relief due to the financial prejudice that she suffered.

In its response to the complaint, the respondent failed to pertinently disprove the complainant's allegations. Furthermore, the respondent failed to produce any record expressly stipulating the basis for its advice as required by section 9 of the GCC.[102]

The court found that the respondent did not make an effort to obtain appropriate and available information from the complainant as required by section 8 of the GCC. Added to that, the respondent did not conduct a needs or risk analysis. According to the Ombud, the advice could hardly be described as appropriate or suitable in the circumstances.[103] The facts indicate that the focus was on selling a policy to the complainant as opposed to rendering a professional

[99] FSA TCF (n 21) 36.
[100] FOC 882/05/KZN/ (1), issued 20 October 2005.
[101] Par 3.
[102] Par 35.3.
[103] Par 39.

service which took her needs and objectives into account.[104] After much consideration, the Ombud held that the respondent's conduct has caused serious financial prejudice to the complainant for which she must be compensated.[105]

This case indicates that behaviour that falls short of the standard required by the FAIS Act is unacceptable. It is again evident that outcome 4 is already embedded in the FAIS Act.

5. Outcome 5: Customers should be provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and what they have been led to expect

It is paramount for the financial adviser or provider to conduct an appropriate due diligence of the product provider before dealing with them, to ensure that TCF principles are also adhered to by the product provider. Product providers should ascertain the performance of products before financial providers transact with customers.

Although this outcome appears to be aimed at product providers when it comes to the performance of products, advisers should not bypass this outcome. TCF require advisers to communicate effectively to their customers the characteristics of the product or service that is being provided.[106] The customers should also be informed – in clear and unambiguous terms – about the range of possible results and experiences one would encounter after obtaining the product. For products which involve market risk for the buyer, there needs to be clarity about the possible impact of, for example, stock market volatility. For general insurance, the insurer should provide clarity about clauses that make provision for exclusions and the likelihood of being able to claim.[107]

For the sake of fairness, any material disclosure by the provider to the consumer should always depict the possible performance of the product. However, the issue of fairness will not be contentious in certain circumstances, for example, when the consumer incurs losses due to equity market falls or when the consumer incurs higher mortgage payments due to the rise of

[104] Par 39.
[105] Par 55.
[106] FSA TCF (n 21) 39.
[107] FSA TCF 13.

interest rates.[108] Once acquired, the service level should at least be acceptable (for example, no undue delays) and certainly it should not be different from the product actually offered.[109]

5.1. TCF outcome 5 aligned with existing FAIS Act obligations

One should take cognisance of the importance of section 6A of the FAIS Act which contains the "fit and proper" requirements that financial services providers should adhere to. The fit and proper requirements may include, but are not limited to, appropriate standards relating to–

a) personal character qualities of honesty and integrity;
b) competence, including–
    i. experience;
    ii. qualifications; and
    iii. knowledge texted through examinations determined by the registrar;
c) operational ability;
d) financial soundness; and
e) continuous professional development.

These standards apply to individuals acting on behalf of the FSPs and FSPs themselves.[110] The primary purpose of the fit and proper requirements is to ensure that the FSP has the ability to provide customers with financial products which perform as they have led the consumers to expect and the services are of an acceptable standard.

Once the financial services provider is equipped with the ability to provide services, it is then imperative for him or her to communicate clearly regarding the financial product, by adhering to all the sections of the GCC which deal with disclosure. One provision in particular is section 7 of the GCC which regulates the manner in which the information of financial services is provided. Section 7 of the GCC requires providers to—

> (a) provide a reasonable and appropriate general explanation of the *nature and material terms* of the relevant contract or transaction to a client, and generally

[108] FSA TCF (n 21) 13.
[109] *Ibid*.
[110] Moolman, Pillai, Bam and Appasamy *Financial Advisory and Intermediary Services Guide* (2010) 28.

make *full and frank* disclosure of any information that would reasonably be expected to enable the client to make an informed decision;

(b) whenever reasonable and appropriate, provide to the client any material contractual information and any material illustrations, projections or forecasts in the possession of the provider;

(c) in particular, at the earliest reasonable opportunity, provide, where applicable, *full and appropriate information* of the following:

…

(vii) *concise details* of *any special terms* or *conditions*, exclusions of liability ... restrictions or circumstances in which benefits will not be provided" (own emphasis).

If the financial services provider adheres to these provisions, any progress made with delivering clear communication and managing their customers' expectations about the products and/or service they are buying, will mitigate issues pertaining to the mis-selling or mis-buying of products.[111]

It is evident that discussions in the previous sections relating to the suitability of advice and products as required by outcome 4 is closely linked to the information given to the client and what was disclosed as required by outcome 3, as unsuitable products will certainly not perform in line with the specific needs a client may have as determined by outcome 2. This results in an obvious correlation between these outcomes which means that the preceding discussions will apply to this outcome as necessary.

5.2. FAIS Ombud case study

5.2.1. *Neil Venter v Daija Investments CC t/a AB Insurance Brokers & Ahmed Bayat*[112]

In casu, the complainant alleged that his insurance claim was rejected by his insurer, following the theft of his Toyota Hilux 2.7 VT.[113] The insurer rejected the claim on the basis that the complainant failed to adhere to the policy condition relating to the testing of the tracking device which was installed in his Hilux.[114] The complainant contends that it was the respondent's non-compliance with the provisions of the FAIS Act and negligent failure to disclose the material term relating to the testing of the tracking device that led to the denial of

[111] FSA TCF (n 21) 39.

[112] FAIS 07999/13-14/GP (3), issued on 11 December 2014.

[113] Par 4.

[114] Par 6.3.

his claim.[115] The Ombud made reference to the provisions of section 7 of the GCC and elaborated that—

> section 7 is about enabling customers to make informed decisions and this is inherent in the principle of treating the customer fairly. Customers should not discover at claim stage that they are bound by provisions of which they were not aware. It is the duty of the provider to disclose all material provisions of a policy to the client and in the circumstances of this case, respondent failed to discharge that duty.[116]

The Ombud firmly contested the explanation by the insurer that the complainant should have availed himself of all the terms and conditions of the policy. The Ombud was appalled at how the respondent had no regard for the FAIS Act or the GCC. The respondent should have adhered to the provisions of the GCC. He cannot simply abdicate his duties and expect his client to fulfil them.[117] Accordingly, the Ombud held that the respondent's failure to comply with the GCC occasioned the complainant's loss and the complaint must succeed.[118]

This case illustrates that a fit and proper person (advisor or intermediary) has a duty to conduct himself in a professional way and part of this entails the ability to identify products that are expected to perform in accordance with a certain standard and to provide services of a quality standard. Knowledgeable intermediaries and advisors should undertake their duties seriously. Again, this TCF principle is already embedded in the FAIS Act.

6. Outcome 6: Customers do not face unreasonable post-sale barriers to change product, switch provider, submit a claim or make a complaint

The consumer ought to be able to change products or switch providers without facing unreasonable obstacles, for example, incurring excessive penalties or being refused to exercise a post-sale right such as a cooling-off right.[119] Firms should try by all means to make the post-sale process as efficient as possible in order to allow consumers to make claims or to complain when something goes wrong.

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[115] Par 6.4.

[116] Par 12.

[117] Par 14.

[118] Par 15.

[119] FSA "Treating Customers Fairly After the Point of Sale" (June 2001) www.fsa.gov.uk/Pages/Library/Policy/DP/2001/discussion_07.shtml (10-10-2015) ("FSA TCF After point of sale").

In the UK, the FSA published a document titled "Treating customers fairly after the point of sale".[120] The primary aim of the document is to highlight the significant work already being done – by the FSA and other bodies – which contribute to the protection of consumers and the fair treatment of retail customers after the point of sale. This document is also aimed at publishing results that were obtained from the research conducted by the FSA in order to address concerns about post-sale barriers.[121]

6.1. TCF outcome 6 aligned with existing FAIS Act obligations

The FAIS Act and the GCC recognise the effects of post-sale barriers within the financial industry. Although this outcome is mainly aimed at product providers, a client's link to the product provider is his or her financial advisor, and specifically where there is an ongoing service between the parties, there is an obligation to assist the client when he or she needs to deal with the product supplier. This can be implied by the fact that the advisor is obliged to do an annual client review in terms of the GCC, during which the client may require a product or portfolio switch, update or adjustment, for which he or she will need the advisor's assistance.

The code also makes provision for the client to submit a complaint to a provider for purposes of resolution by the provider.[122] In terms of section 16(2) of the GCC:

> [A] provider must—
>
> a) request that any client who has a complaint against the provider must lodge such complaint in writing;
> a) maintain a record of such complaints for a period of five years;
> b) handle complaints from clients in a timely and fair manner;
> c) take steps to investigate and respond promptly to such complaints; and
> d) where such a complaint is not resolved to the client's satisfaction, advise the client of any further steps which may be available to the client in terms of the Act or any other law.

The GCC also requires certain basic internal complaint resolution system and procedures to be established and maintained by the provider in accordance with this provision for the resolution of complaints by clients. Section 17 of the GCC stipulates that

[120] *Ibid*.

[121] *Ibid* Annex C.

[122] Section 16 (2) of the GCC.

[A] provider, excluding a representative, must maintain an internal complaint resolution system and procedures based on the following:

a) Maintenance of a comprehensive complaints policy outlining the provider's commitment to, and system and procedures for, internal resolution of complaints;
b) transparency and visibility: ensuring that clients have full knowledge of the procedures for resolution of their complaints;
c) accessibility of facilities: ensuring the existence of easy access to such procedures at any office or branch of the provider open to clients, or through ancillary postal, fax, telephone or electronic helpdesk support; and
d) fairness: ensuring that a resolution of a complaint can during and by means of the resolution process be effected which is fair to both clients and the provider and its staff.

This outcome is recognised by the FAIS Ombud and enforcement measures are prescribed for non-compliance. Although this dissertation had difficulty identifying the most appropriate example of a FAIS Ombud case dealing with this outcome, a fictional case study has been provided below to illustrate an instance where this outcome will be taken into consideration by FAIS Ombud.

6.2. FAIS Ombud case study

6.2.1. The case of 'Mr D'[123]

A complainant had invested a substantial amount of money in a Bond Fund. The complainant was relatively close to retirement, she decided to approach her personal financial advisor (respondent) to discuss the possibility of switching products. The respondent recommended that the complainant should switch all the funds to a defensive portfolio. The complainant had subsequently approached the respondent and had been advised that she could send the switch instruction via e-mail. The complainant sent the respondent an e-mail requesting that her pension proceeds be moved to a Defensive Fund. A year later, the complainant discovered that her instruction to switch products had never been actioned by the respondent, and according to the complainant she had sustained losses. After approaching the respondent, she was offered a settlement value. The respondent refused to improve on the original offer because it

[123] FAIS Ombud "Under the baobab tree" 2015 http://www.faisombud.co.za/sites/default/files/FAIS%20Newsletter%20Issue%208.pdf (29-10-2015).

felt that the complainant was also at fault because she failed to follow-up to ascertain that the switch had been actioned.

In officially accepting the matter for investigation the Ombud confirmed that the respondent had by its own admission confirmed that it had erred in not advising the complainant of the correct procedure to request a switch and that it was as a result of this omission that the switch had not been actioned. In its ruling, the Ombud advised that firms should ensure that they always determine the correct procedure for submitting a request to switch portfolios. Most product providers have specific switch request forms and the mere submission of an email may not suffice.

Even in any other given situation, if the respondent had advised the complainant of the correct procedure to request a switch, the FAIS Ombud will not take lightly to clients being locked into an agreement. This means that that it should be possible for a client to make an informed decision even after a product has been purchased.

Chapter 3: Fairness in the greater financial services industry

1. Introduction and background

Enough discussion has been dedicated to proving that TCF is already embedded in the FAIS Act and that it is not a magical wand. In fact, if one scrutinises common-law principles pertaining to the law of agency and representation that were in existence before the introduction of the FAIS Act, it is evident that fairness is not a new concept. For instance, the duty to act with reasonable *care and skill* and to act in *good faith* has always formed the basis of our financial intermediary and advisory services.[124] Added to that, there were also additional, more polished rules in place which regulated intermediary services and advice in specific industries before the introduction of the FAIS Act.[125] For instance, duties of a broker were inherent in our common law which necessitated brokers to execute those duties with reasonable care and skill. Some of these duties required a broker to prepare the policy wording, to assist the insured to disclose material information, to deliver the policy, or a copy, or a summary of the policy to the insured, to advise the insured as to the meaning of the policy, to advise the insured that cover has lapsed, not to cancel the policy without the necessary authority, to assist with the claim, and so forth.[126]

A close observation of these duties indicates that the FAIS Act gathered rules pertaining to intermediaries and advisors and placed them under a legislative umbrella and prescribed them as codes of conduct which are specific to each type of service or advice.[127] One should not be mistaken to think that the FAIS Act has materially changed the common law. All that the FAIS Act did was to take common-law duties and refine them into clear rules with the effect that compliance with the rules would illustrate that an advisor or intermediary had acted with the standards of care and skill and in good faith.[128] These clear standards have the effect of entrenching consumers' rights and attaching consequences to non-compliance.[129]

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[124] Hattingh and Millard (n 26) 81.
[125] *Ibid* 85.
[126] *Ibid* 80-81.
[127] *Ibid* 85.
[128] *Ibid*.
[129] *Ibid*.

It is significant to note that the FAIS Act – together with the GCC – stipulates that a FSP should act "honestly and *fairly*, and with due skill, care and diligence" (emphasis added). This indicates that the regulator has done away with the concept of good faith and opted to use the concept of fairness. Whether or not there is a difference between these two concepts is beside the point of this dissertation. However, it is worth noting that the very notion of fairness has left regulators, policy makers, academic authors, judicial officers, FSPs and consumers in much discomfort due to its abstract nature. The discomfort also stems from the fact that our legal framework already embodies the concept of fairness in statutes, public policy and various other initiatives such as the recent TCF approach. With regards to TCF, Georgosouli attests that TCF is arguably "more flexible, adaptable, participatory, and dialectical and, therefore, more suited to instituting long-term cultural change regarding the way in which retail firms perceive their relationship with their customers and what 'fair treatment' entails in practice".[130] If one considers some of these compelling statements made about TCF, it would seem unfounded for financial institutions to gainsay the TCF initiative.

However, this dissertation is disposed to be in support of the view shared by Smith that "there is a growing sense that behind TCF's uncontroversial, 'motherhood and apple pie' facade lies dangers for both financial institutions and their customers".[131] This view is not intended to suggest that TCF is not capable of engendering high levels of trust and confidence in the market place and most importantly to promote fairness; however, it aims to suggest that TCF might just be a mere addition to other "fairness" standards. This craze of fairness is bound to confuse financial institutions about what is expected from them and it might also confuse regulators and courts in terms of how to regulate the notion of fairness.

In the following sub-paragraph, this dissertation will briefly look at some of the regulations that have been imposed by the FSB which contribute to this craze of *fairness*.

2. Examples of provisions requiring fairness in the financial services industry

Regardless of the fact that fairness has been vague and abstract for many years, the FSB still insists on incorporating this concept in its regulatory and initiative framework. For example, the

[130] Georgosouli (n 22) 425.

[131] Smith "Financial regulatory developments" 2007 *Law and Financial Markets Review* 161.

Code of Banking Practice (CoBP) is a noteworthy voluntary code that was implemented in 2012 which sets out the minimum standards for service and conduct that a consumer can expect from their banks with regards to the services and products the banks offer and how the banks conduct themselves towards consumers. The banks are required to "act *fairly*, reasonably and ethically" in all their dealings with a consumer or potential consumer (emphasis added).[132]

Under the Financial Markets Act (FMA),[133] the Act endorses certain minimum standards and indicates that regulated persons should "act honestly and *fairly*, with due skill, care and diligence and in the interests of a client" (emphasis added).[134] In the same light, as mentioned in the preceding chapters, the FAIS Act also places certain duties on financial advisors and intermediaries to "act honestly, *fairly*, with due skill, care and diligence and in the interest of the client and the integrity of the financial services industry" (emphasis added).[135]

In addition to all of this, the FAIS Ombud is required to consider customer complaints in a "procedurally *fair*, informal, economical and expeditious manner and by reference to what is equitable in all the circumstances…"(emphasis added).[136] However, before a disgruntled client approaches the Ombud or decides to resort to litigation, the service provider must have failed to adhere to the requirements of the GCC pertaining to the internal resolution of complaints.[137] Therefore, when it comes to regulating the internal resolution complaints, the GCC stipulates that a provider has, amongst others, a primary obligation to handle complaints from clients in a timely and *fair* manner.[138] Apart from this primary obligation, the provider needs to ensure that *fairness* is one of its basic principles when dealing with complaints.[139]

[132] Par 3.1 of the Code of Banking Practice.

[133] 19 of 2004.

[134] Section 75 of the FMA. "Fairness" in the financial markets has a different meaning to when the term is applied to conducting business. In the financial market context it refers to investors, when buying and selling securities, having access to the same information at the same time, so that they may assess the risk-weighted value of that asset. Investors who have more information than others will have an unfair advantage, and can unfairly "game" the system.

[135] Section 16 of the FAIS Act.

[136] Section 20(3) FAIS Act.

[137] Millard (n 30) 242.

[138] Section 16(2)(c) of the GCC.

[139] Section 17(d) of the GCC. See also Millard (n 30) 242.

To add to the confusion, the FSB is in the process of finalising the Retail Distribution Review document (RDR) which focuses "primarily on achieving improved outcomes for retail financial customers, who are most vulnerable to the risks of *unfair* and conflicted advice and sales practices, due to the inherent information asymmetry and financial capability risks they face" (emphasis added).[140] One of the RDR's primary objectives is "to ensure that the definitions of intermediary services and related remuneration structures in the insurance sector should promote appropriate, affordable and *fair* advice and services to potential and existing policyholders" (emphasis added).[141]

From the discussion in the two sub-paragraphs above, it is clear that fairness has been used as a mystical yardstick by courts and regulators to regulate the conduct of advisors and intermediaries within the financial services industry. Before the inception of the FAIS Act up until today's twenty-first century, it seems as if fairness is gaining more momentum world-wide.

3. A critical analysis of the concept of fairness

It is a common fact that when people transact, their primary goal is to obtain the most favourable outcome. At the very least, people work to achieve outcomes that they can call fair, and particularly "fair enough to me!"[142] What is fair to one person could disparately be different from another person's perception of fairness.

The issue of fairness raises a few key questions. Firstly, whether financial institutions understand what fairness really means and the extent to which their conduct can be classified as fair treatment of customers. Secondly, whether consumers' perception and views of what constitutes fairness is envisaged by policymakers, regulators and the courts. Thirdly, whether the regulators and the courts will interpret the varying requirements of fairness in a manner that is equitable, fair and just. "More disconcertingly still, are regulators using 'fairness' fairly?"[143]

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[140] Financial Services Board "Retail Distribution Review" 2014 https://www.fsb.co.za/NewsLibrary/FSB%20Retail%20Distribution%20Review%202014.pdf (21-10-2015).

[141] *Ibid* 9.

[142] Welsh "Perceptions of fairness in negotiation" 2004 *Marquette Law Review* 753.

[143] Smith (n 131) 161.

There are different ways of contextualising fairness. Fairness is much more versatile than the mere definition contained in the Oxford dictionary which states that fairness is "the quality of treating people equally or in a way that is reasonable".[144] For example, fairness involves placing clear, basic information and guidelines at the consumer's disposal in order for him or her to freely navigate choice and quality in modern markets and public services without any undue influence from the regulator or the financial institutions. Fairness could also suggest that no party – especially the financial institution – entering into a transaction with another should have an upper hand in markets and public services, which could ultimately have the potential implication of exploiting the other. Furthermore, one could assert that fairness is a measure that is aimed at isolating and preventing circumstances which are so bleak that a particular consumer cannot be expected to make certain choices wisely.

On the other hand, Kahneman, Knetsch and Thaler considered the role of fairness in matters relating to economics.[145] They set out to evaluate whether a firm's standard economic model of pricing products or services is fair or not based on community standards (i.e. standards of decency). Put differently, that fairness is simply what a community perceives as fair or unfair.[146] Their contribution consisted of a sequence of three studies which were put to a general population in order to identify some of the criteria that people use in their fairness judgments and to demonstrate the willingness of people to resist unfair firms at some cost to themselves.[147] Kahneman, Knetsch and Thaler advised that a customer's perception of fairness will not be satisfied if a firm merely applies a standard economic model or a simple cost-plus rule of thumb when pricing its products or services.[148] It was established that consumers will consider prices fair if, for example, firms give apt consideration to past prices on particular goods before increasing prices.[149]

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144 Hornby (ed) *Oxford advanced learner's dictionary* (2005) 526.

145 Kahneman, Knetsch and Thaler "Fairness and the assumptions of Economics" 1986 *Journal of Business* 285.

146 *Ibid* 285-287.

147 *Ibid* 285.

148 *Ibid* 299.

149 *Ibid* 297. Reference transactions such as past prices simply mean that customers would normally consider it unfair for firms to mark-up products or services without having an appropriate justification for the increase. An increase should be reasonable considering the last placed price on a particular product.

But enough of economics. To return to the role of fairness and the law, it is significant to note the sentiments expressed by Brynard regarding the principles of fairness. Brynard convincingly stated that "[f]airness is not something that can be reduced to a one-size-fits-all formula. Instead, fairness is a nuanced assessment of the demands imposed by a particular situation".[150] What is fair is dependent on the circumstances of each case. Brynard considered the role of fairness with the intention of clarifying the position of procedural fairness.[151] Procedural fairness is concerned with the processes implemented by an institution in reaching its decision (i.e. a fair and proper procedure followed) and does not relate to whether the decision itself is fair or not.[152] However, the process implemented by a firm will be considered fair if it incorporates elements such as impartiality, refutability, explanation and familiarity.[153]

Besides procedural fairness, distributive and interactive fairness also have the potential of influencing the role of fairness in the financial services industry. Distributive fairness is an intuitive assessment of whether a person has been allocated an outcome which is fair or unfair.[154] Interactive fairness refers to elements that characterise the manner in which institutions interact with consumers. These elements include truthfulness, friendliness, interest, honesty, efforts put in to resolve the conflict, courtesy, respect, consideration and the degree of bilateral communication.[155]

Aggarwal and Larrick observed various academic studies in order to establish the interaction between these three types of fairness perception.[156] The first part of the findings indicated that people are more concerned with the overall outcome that is allocated to them (distributive fairness) rather than the procedures utilised by an institution (procedural fairness).[157] A

[150] Brynard "The duty to act fairly a flexible approach to procedural fairness in public administration" 2010 *Administratio Publica* 126.

[151] *Ibid*.

[152] *Ibid*.

[153] Worthington and Devlin "Fairness and financial services in Australia and the United Kingdom" 2013 *International Journal of Bank Marketing* 292.

[154] Welsh (n 142) 87.

[155] See Worthington and Devlin (n 153) 292. See also Aggarwal and Larrick "When consumers care about being treated fairly: The interaction of relationship norms and fairness norms" 2012 *Journal of Consumer Psychology* 117.

[156] Aggarwal and Larrick (n 155) 117.

[157] *Ibid*.

consumer will most likely be more concerned with procedural fairness when facing unfavourable outcomes than when facing favourable outcomes.[158] The second part of the findings revealed a similar interaction between distributive fairness and interactional fairness.[159] They note that interactional fairness matters more when someone has experienced an unfavourable outcome rather than a favourable outcome.[160] In fact, when the outcome is positive, people may not resent the decision maker as much for low interactional fairness—"at least the final result was fine!" one may say.[161]

It would come as no surprise if one could refer to the above tenets of fairness and still be uncertain of the perception of "what is fair". Fairness has different definitions which make it difficult for anyone to capture its true essence in one simple, straight-to-the-point definition. Considering the diverging views regarding fairness, this dissertation seeks to stress the question of whether the implementation of TCF in South Africa will be able to clarify the meaning of fairness. Or rather, will it make it any easier for stakeholders in the financial services industry to understand and apply the concept of fairness?

4. Understanding the perception of fairness according to consumers

From the discussion in the above sub-paragraph, it is clear that the question of "what is fair" is still an ongoing debate. However, one cannot gain guidance by relying solely on what regulators, policymakers and institutions think about fairness – this will not settle the debate. The very same people who need to be treated fairly need to be consulted with in order to help understand their perception and views on what constitutes fairness in their dealings with providers of financial services.

In the UK, the FSA conducted research which culminated in a document titled "Financial Services Authority Treating customers fairly: the consumers' view"[162] in order to gain insight

[158] *Ibid*.
[159] *Ibid*.
[160] *Ibid*.
[161] *Ibid*.
[162] Financial Services Authority *Treating Customers Fairly: The consumers' view* (2005) http://www.fsa.gov.uk/pubs/consumer-research/crpr38.pdf (21-10-2015) (FSA TCF consumer's view).

into consumers' perception of fairness.[163] The research unpacked a series of principles which emerged across the whole programme, providing the FSA with a summary framework of the consumer's perspective on fairness.[164]

These principles are as follows, namely:

1. give the customer what they have paid for;
2. do not take advantage of the consumer;
3. offer the customer the best product you can;
4. do your best to resolve mistakes as quickly as possible;
5. show flexibility, empathy and consideration in dealing with customers; and
6. exhibit clarity in all customer dealings.

These principles demonstrate the basic expectations that consumers hold when interacting with financial institutions. Also, these expectations stem from the fact that consumers feel potentially vulnerable to unfair treatment because they do not have the knowledge or experience to identify it, and they see this as making it relatively easy for providers to treat them unfairly.[165]

Institutions should not be mistaken by thinking that consumers have an "I don't care" attitude when it comes to identifying fairness judgements. Consumers actually care about being treated fairly and treating others fairly.[166] They are willing to resist unfair firms even at a positive cost and they have a common view of actions of firms which are considered fair or unfair.[167]

Let us assume that the FSA decided to replace the current six TCF fairness outcomes with the six principles underpinning the consumer's perspective of fairness. Would it still be substantiated if one had to argue that the FAIS Act already encapsulates the latter six principles? The answer would be "yes". Over and above anything, section 16(1)(a) of the FAIS

[163] Prepared for the Financial Services Authority by TNS Financial and Professional Services. The TNS project team comprised of Paul Stamper, Director, Vicky Korn and Juliette Livesey.

[164] FSA TCF consumers' view (n 162) 2.

[165] *Ibid* 34.

[166] Kahneman, Knetsch and Thaler (n 145) 299.

[167] *Ibid*.

Act prescribes that a provider “must at all times render financial services honestly, fairly, with due skill, care and diligence, and in the interest of clients and the integrity of the financial services industry”. This general provision has far-reaching application and adherence to this provision is enough to support all these principles. In addition to that, specific provisions such as disclosure and internal and external complaint resolution systems have already been covered by the FAIS Act and its GCC.

Chapter 4: Fairness in contracts and the way forward

1. Introduction: legal certainty

South African private law, of which contract law is a part, is essentially uncodified.[168] This means that seventeenth-century Roman-Dutch law still lies at the core of this uncodified system.[169] This then led to legal certainty becoming a foundational principle of the South African legal system. Legal certainty entails that the law must be certain in order to enable legal subjects to regulate their dealings within the private sphere. And because new circumstances are inevitable, the law becomes forced to adapt to changing social needs and values and the most efficient way to bring about change is to enact legislation (e.g. the Consumer Protection Act,[170] National Credit Act,[171] and Protection of Personal Information Act[172] (POPI)).[173] Another way to develop the law is for the judiciary to modify, extend or supplement common-law principles. Although the system of precedent or *stare decisis* serves as another medium to develop the common law, its very nature does not lend itself to radical change. [174] The system itself has an inherent restraint, because judges who develop or change the law end up creating precedents for similar cases that follow.[175] It should be borne in mind that developing the common law is an expectation required in terms of section 39(2) of the Constitution.[176] Courts must adapt the common law in accordance with the spirit, purport, and objects of the Bill of Rights.

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[168] Brand "The role of good faith, equity and fairness in the South African law of contract: The influence of the common law and the Constitution" 2009 *SALJ* 71.

[169] *Ibid* 71.

[170] 68 of 2008.

[171] 34 of 2005.

[172] 4 of 2013.

[173] Brand (n 168) 72.

[174] *Ibid*.

[175] *Ibid*. It has been said that *Everfresh Market Virginia (Pty) Ltd v Shoprite Checkers (Pty) Ltd* 2012 1 SA 256 (CC) is an example of a case that missed the opportunity to develop the duty to negotiate in good faith beyond precedent. See Mupangavanhu "Yet Another Missed Opportunity to Develop Common Law of Contract? An Analysis of *Everfresh Market Virginia (Pty) Ltd v Shoprite Checkers (Pty) Ltd* (2011) ZACC 30" 2013 *Speculum Juris* 148 150 for more information.

[176] Section 39(2) of the Constitution provides: "When interpreting any legislation, and when developing the common law or customary law, every court, tribunal or forum must promote the spirit, purport and objects of the Bill of Rights".

2. Critical analysis of using the Constitution to infuse fairness in contracts

TCF is an ambitious project aimed at the furtherance of consumer protection.[177] However, TCF defeats the purpose of legal certainty because it currently exists as a mere project and does not have the status of a binding statute or a code or regulation in terms of a statute.[178] In addition to that, the policy decision to depart from a rule-based approach and to resort to TCF as a direct and informal means of communicating regulatory stipulations is bound to escalate the confusion relating to the taxonomy of what is fair.[179] In chapter 3 of this dissertation, reference was made to the problematic nature underpinning the concept of fairness. This present discussion is set to elaborate further on how courts have been grappling with the same issue and find it difficult to give content to the concept of fairness.[180]

The day when *exceptio doli generalis* was abolished in *Bank of Lisbon and South Africa Ltd v De Ornelas*,[181] courts resorted to the concept of public policy as an alternative to introduce fairness and good faith into our law of contracts. However, the majority case in *Brisley v Drotsky*[182] did not allow the notions of good faith and fairness to easily override the principle of *pacta sunt servanda*. In *casu*, the majority held that good faith, reasonableness and fairness are not independent, substantive rules that allow courts to intervene in contractual relationships.[183] Rather, these abstract values perform creative, informative and controlling functions through the rules of contract law. In addition, courts can only interfere with contractual relationships if the rules of hard law permit this. Furthermore, if judges refuse to enforce a contractual provision merely because it offends their "personal sense of fairness and equity", this will give rise to "intolerable legal and commercial uncertainty".

[177] Georgosouli (n 22) 420.

[178] Millard "Through the looking glass: Fairness in insurance contracts – a caucus race?" 2014 *THRHR* 548 549.

[179] Georgeosouli (n 22) 420.

[180] Millard (n 178) 566.

[181] 1988 3 SA 580 (A). *Exceptio doli generalis* was the Roman-law defence of 'bad faith' which gave courts an equitable discretion to transport abstract values of fairness and equity into our substantive contract law.

[182] 2002 4 SA 1 (SCA) par 21–25 and 93–95.

[183] Par 22.

When the Supreme Court of Appeal had to decide whether to enforce an exemption clause in *Afrox Health Care Ltd v Strydom*[184] which was aimed at absolving the hospital from liability for damages arising from the negligence of its nursing staff, the court re-iterated, as in *Brisley v Drotsky*, that good faith, reasonableness and fairness "do not provide an independent, free-floating basis for interfering with contractual relationships".[185] However, it is worth noting that, for the first time, the *Afrox* case invoked the Constitution as the main source of public policy when *Strydom* relied on section 27(1)(a) of the Constitution, which guarantees the right of every person to medical treatment.[186] On the facts, the court found that there was no factual evidence of an infringement of a constitutional right and effectively ruled in favour of the *pacta sunt servanda* principle.

Just like in the case of *Brisley*, the Supreme Court of Appeal in *Afrox Health Care Ltd v Strydom*, and *Barkhuizen v Napier*,[187] endorsed the concept of public policy as a "doctrinal gateway for the importation of constitutional values into the law of contract".[188] When *Barkhuizen* went on appeal to the Constitutional Court, the court adopted the approach in which the Constitution was used as a vehicle to import good faith, equity and fairness into South African contract law. This means that any contractual provision which contravenes the values enshrined in the Constitution will be regarded as contrary to public policy and consequently unenforceable.

In *Barkhuizen*, the contractual term under scrutiny stipulated that if the underwriter rejects liability for any claim made under the policy, they would be released from liability unless summons is served within 90 days of repudiation.[189] One of the issues in dispute was whether the time-limitation clause was unconstitutional and unenforceable because it violated Barkhuizen's right under section 34 of the Constitution, which guarantees free access to an independent tribunal.[190] Ngcobo J posed two questions before the court: the first was whether

[184] 2002 6 SA 21 (SCA).
[185] Brand (168) 81.
[186] Brand (168) 81.
[187] 2006 (4) SA1 (SCA).
[188] Brand (168) 84.
[189] Par 3.
[190] Par 8.

the clause was unreasonable, and secondly, if the clause was reasonable, whether it should be enforced in light of the circumstances which prevented compliance with the time-limitation clause.[191] Ngcobo J concluded that the 90 day limitation was not manifestly unreasonable, nor was it manifestly unfair.[192] It was held that public policy tolerated time-limitation clauses subject to the considerations of reasonableness and fairness.[193] Therefore, if a contractual term provided for an impossibly short time for the dispute to be referred to a court of law, it would be contrary to public policy and unenforceable.[194]

Initially, Brand was inclined to concur with *Brisley* and *Afrox* when they affirmed their support for the principle of *pacta sunt servanda* over fairness. Not only did these courts indicate that the sanctity of contracts is aimed at promoting legal and commercial certainty by enforcing contracts that are freely and properly entered into by the parties, but they also highlighted the very premise of contractual autonomy which was held to be founded on the constitutional values of dignity and freedom.[195] Brand reconsidered this view and later concurred with other academic authors who criticised this view on the basis that "it over-emphasizes the 'empowerment based' aspect of dignity while at the same time ignoring another aspect of dignity, namely that aspect which demands that a human being should never be treated as the means to an end, but always as an end in itself, and this imposes a limitation on the contractual freedom of the other party".[196] Despite the fact that the values of dignity and freedom display the capacity to meander in several directions at the same time and may accordingly fulfil very different roles, Brand is of the opinion that good faith cannot operate by finding a specific constitutional value, expressly referred to in the Constitution, to underpin every rule of contract law.[197] He firmly believes "the concept of public policy needs development and fine tuning" in order for courts to provide for "the changing needs and values of society by incremental change without creating wholesale legal and commercial

[191] Par 56.

[192] Par 60.

[193] Par 63.

[194] Par 67.

[195] Brand (n 168) 85.

[196] Brand (n 168) 86 referred to in Lubbe "Taking fundamental rights seriously: The bill of rights and its implications for the development of contract law" 2004 121 *SALJ* 359 at 420.

[197] Brand (n 168) 87. See also Cornelius (n 181) 89-90.

uncertainty".[198] This means that matters of fairness and good faith need to be accommodated under the rubric of public policy to encourage the process of "fine tuning".[199]

Mupangavanhu considered the question of whether fairness and equity are fully accommodated under the rubric and scope of public policy. Just like Brand, he is of the opinion that public policy needs further development to fully accommodate fairness and equity.[200] Mupangavanhu highlights a seminal judgment of why public policy is lacking in its current application. Judging from case laws such as *Brisley* and *Afrox*, he states that public policy is lacking in its current application because it has proven that it favours freedom of contract and is based on the understanding that commercial transactions should not be unduly trammelled by restrictions of that freedom.[201]

3. Commentary: proposed way forward

The provisions of the FAIS Act and GCC (and other financial services regulations) – together with the common-law principles – are capable of forcing courts as well as financial institutions to be in conformity with the common-law principles of care and skill and good faith. Hattingh and Millard sufficiently explain this point by stating that "[t]he true value of the FAIS Act, as with the Constitution, lies in the fact that it entrenches principles that had existed previously in legislation, thereby enhancing the rights of those who stand to suffer as a result of an infringement of those rights".[202] The FAIS Act was on the right track when it gathered rules pertaining to advisors and intermediaries under one umbrella and by prescribing codes of conduct which are specific to each type of service or advice in order to assist role players in knowing what is expected of them along the road to compliance with the Act, thereby ensuring that there is at least a *minimum standard of care and skill* and *fairness.*

However, the effectiveness of the FAIS Act, GCC and other regulations gradually became undermined by the legislator's failure to clarify provisions and concepts such as fairness, which

198 Brand (n 168) 87-88.

199 *Ibid* 87.

200 Mupangavanhu "Fairness a slippery concept: The common law of contract and the Consumer Protection Act 68 of 2008" 2015 *De Jure* 125. See also Brand (n 168) 87.

201 Mupangavanhu (n 200) 125.

202 Hattingh and Millard (n 26) 89.

are vague and ambiguous. And for the FSB to introduce TCF with the aim of ameliorating the problems of treating customers unfairly will not sufficiently ensure adequate outcomes because the initiative itself is also capsuled in vague terms such as fairness.

Fairness is a slippery concept which is not easy to attain,[203] its abstract nature infuses discomfort in various regulatory systems. Just like the concept of good faith, it has been said, amongst other things, that the very notion of good faith (and fairness) is too vague; it means different things to different people in different moods at different times and in different places; and it can serve as an invitation to judges to abandon the duty of legally reasoned decisions and to produce an unanalytical incantation of personal values.[204] However, the answers to these underlying concerns were adequately addressed by Clarke a few years back when he noted a number of these objections raised against the general doctrine of good faith. He said that the concept of good faith (and fairness) is misunderstood by many because regulators and courts tend to think that these concepts are rules.[205] He goes further to clarify that these concepts are not rules but standards, which are not applied without more but which require concretisation through the judicial creation of certain rules.[206] This means that fairness as a standard will be effective if specific and comprehensive rules are formulated to impose a requirement on businesses to act fairly. Put simply, the regulator should strive to regulate fairness matters by name. This view has been considered by the South African Law Commission (SALC) in its Project 47 report titled "Unreasonable stipulations in contracts and the rectification of contracts" published in 1998.

Just like the SALC, the New Zealand Law Commission (NZLC) also expressed its support for expressly stipulating market conduct abuses in terms of standards that have some subjective element to it.[207] The NZLC further elaborated by stating that consideration should be given to

[203] Mupangavanhu (n 200) 135.

[204] Clarke "The common law of contract in 1993: Will there be a general doctrine of good faith?" Law Working Paper Series Paper no. 8 (February 1993) 25-28 http://hub.hku.hk/bitstream/10722/54906/2/31801482.pdf?accept=1.

[205] *Ibid* 28.

[206] *Ibid*.

[207] The South African Law Commission "Unreasonable stipulations in contracts and the rectification of contracts" Paper 47 (1998) 123-145 referred to the New Zealand Law Commission *Unfair Contracts* at 28.

the idea of specifying particular terms that may be considered unfair, and particular circumstances under which the courts may intervene on this ground.

For example, the case of *Barkhuizen* was conflicted with whether the time-limitation clause was reasonable. Had there been a rule that expressly regulates time-limitation clauses by specifying what is objectionable or fair, then courts would have been in a better position to adjudicate on the matter. In the case of *Afrox*, a question was posed whether an exemption clause that excluded liability for any damages suffered as a result of the negligence of the nursing staff was substantively fair. Had there been a rule that sets constraints on exemption clauses then maybe the court in *Afrox* would have been able to reach an equitable decision. This then means that rules should be created that will regulate the inclusion of exemption clauses in contracts as well as other rules regulating matters such forfeiture clauses, disclaimer notices, cancellation clauses[208] and restraints of trade.[209]

It is important to consider countries such as the United States of America, the UK and Hong Kong which have set defined parameters to conceptualise the concept of good faith.[210] They felicitously conceptualised good faith as an "excluder" which was aimed to "rule out a wide range of heterogeneous forms of bad faith".[211] This means that good faith is described only by saying what it is not – misrepresentation, economic duress, abuse of stronger bargaining position and so on.[212]

One of the advantages of drafting specific rules is that it leads to the possibility of accelerating compliance under a general obligation to develop the common law by applying constitutional values as mandated by sections 8(3), 39(2) and 173 of the Constitution.[213] Going forward, courts should insist on developing the common law by infusing FAIS values throughout

[208] *Botha v Rich* 2014 4 SA 124 (CC).

[209] *Knox D'Arcy v Shaw and another* 1996 2 SA 651 (W) and *Polygraph Center – Central Provinces CC v Venter and another* (2006) All SA 612 (O).

[210] Clarke (n 204) 29.

[211] *Ibid*.

[212] *Ibid* 30.

[213] *Carmichele v Minister of Safety and Security* 2001 4 SA 938 (CC) par 39: "It needs to be stressed that the obligation of courts to develop the common law, in the context of the section 39(2) objectives, is not purely discretionary. On the contrary it is implicit in section 39(2) read with section 173 that where the common law as it stands is deficient in promoting the section 39(2) objectives; the courts are under a general obligation to develop it appropriately."

the product life-cycle of a transaction. Added to that, the value of *Ubuntu* should "inspire much of our constitutional compact".[214] Absolute emphasis on the freedom and sanctity of contracts should be limited and fairness and equity should prevail.

The penultimate advantage is that the issue of uncertainty will not be exacerbated due to the defined limits which would prescribe what is fair or unfair. Added to that, the set criteria will not burden people to rely strictly on the rules but it will also allow them to take risks where they wish to. However, people will be cautioned to take risks in light of principles of fairness and reasonableness

The ultimate advantage is that courts will be cautioned from relying directly on the Constitution as a "notorious magic wand" aimed to solve anything and everything that offends our public policy. Our Constitution should be viewed as being sacred and anyone who decides to rely on it should do so in exceptional cases.

4. Conclusion

The TCF initiative is convincing and morally compelling. However, whether or not South Africa is in dire need of it is highly questionable. TCF shares the same ultimate goal with the FAIS Act, and other regulations, which is to ensure the fair treatment of customers. Added to that, the same TCF fairness principles are already embedded within regulations such as the FAIS Act. In fact, as was illustrated, common law that was in existence before the enactment of FAIS Act already included principles of fairness that underpinned the relationship between financial advisors, intermediaries and the client.

As this dissertation so easily illustrates, one can safely hold that the prospect of TCF producing excellent results beyond what the FAIS Act already provides for is unfounded. As a matter of fact, the FSB is setting impossibly high expectations by thinking that the shift towards broadly stated principles rather than more detailed rules will guarantee the attainment of market conduct objectives. The reason why TCF will not make a huge impact in South Africa's financial sector is because it is a premature initiative that is not adequately contextualised in

[214] As held by Moseneke DCJ in *Everfresh Market Virginia (Pty) Ltd v Shoprite Checkers (Pty) Ltd* [2011] ZACC 30 par 72.

South African law. Its failure to help clarify the meaning of fairness will be fatal to its own fairness outcomes.

Going forward, the regulator should consider introducing clear, specific rules by name which will be aimed at regulating specific services and products within the financial services industry. After all, fairness is an objective standard that is capable of being applied at all phases of a product life-cycle subject to the legislature specifying particular terms that may be considered fair or unfair.

5. List of abbreviations

CoBP	Code of Banking Practice
CPA	Consumer Protection Act
FAIS	Financial Advisory Intermediary Services
FMA	Financial Markets Act
FSA	Financial Services Authority
FSB	Financial Services Board
FSMA	Financial Services and Markets Act
FSP	Financial Services Provider
FSR	Financial Sector Regulation
GCC	General Code of Conduct
NCA	National Credit Act
NCR	National Credit Regulator
NZLC	New Zealand Law Commission
POPI	Protection of Personal Information Act
RDR	Retail Distribution Review
SALC	South African Law Commission
SARB	South African Reserve Bank
TCF	Treating Customers Fairly
UK	United Kingdom

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