CAN YOU SUE A BAD INVESTMENT ADVISOR? IT DEPENDS...

"I always advise people never to give advice" (P. G. Wodehouse)

If you want to send shivers down the spine of any investor, mention "Steinhoff", or "Sharemax", or any one of the many other spectacular corporate collapses that have plagued both local and overseas investors in recent times.

Quite apart from the high-profile failures it's been a hard few years for investors generally, and if your nest egg has taken a painful tumble recently you may well wonder whether you can sue your financial advisor for giving you bad advice.

The short answer, as several recent cases have highlighted, is "It depends…".

Case 1: A R2.5m claim succeeds

A widow, still reeling from her husband's death and unversed in financial products, invested R2m in Sharemax on the advice of her trusted financial advisor, an authorised Financial Services Provider (FSP).

She made it clear that she needed a safe, low risk investment and "that she could not risk losing even two cents as the money was earmarked for her son's upbringing".

The advisor did not explain any other investment products and emphasized that "it was so good that he did not even want to introduce other financial instruments and/or investments to her."

Sharemax of course collapsed, and the investor duly sued the advisor for her R2m plus interest - a total of almost R2.5m by the time this case found its way through the High Court and an appeal to the Supreme Court of Appeal (SCA).

The advisor was found liable on the basis of having been negligent "and even dishonest" and to have "failed to exercise the degree of skill, care and diligence which one is entitled to expect from a FSP".

Case 2: An R11m claim fails

A UK couple temporarily in South African sought a local financial advisor's advice on how best to invest some "spare cash".

They ended up putting GBP 565,000 and R700,000 (about R11m in all) into investment products offered by UK based investment companies. The companies failed and the investments were rendered worthless.

The investors successfully sued the advisor in the High Court for R11m in damages, but on appeal to the SCA their claim was dismissed.

The investors, said the Court, had failed on the evidence to "identify what a reasonably skilled financial service provider would know about products in the market place; what due diligence they would have done before making a presentation to a prospective client and what sources of information they would have consulted." They had failed to prove that any negligence on the advisor's part in "making a presentation without adequate knowledge of the proposed investments, resulted in advice materially different from that which a reasonably competent advisor would have given." (Emphasis supplied).

End result - the investors lose their R11m and face a (doubtless substantial) legal bill.

Case 3: A R5m claim fails

To the High Court now for some insight into the range of factors that a court is likely to take into account in deciding liability –

This was another Sharemax investment, this time for R5m.

The difference was that this investor was found to have been an astute and wealthy businessman who managed his own share portfolio and went into the investment understanding the risks and "with his eyes open" after taking independent advice.

Claim dismissed.

The bottom line, and some advice for investors

Let's start off with this thought - unless you are fully qualified to make your own investment decisions, seeking help from a financial advisor is a no-brainer. A trained and certified professional advisor brings elements of insight, knowledge and objectivity that you can never match on your own.

Just be sure that your chosen advisor is the right advisor for you and is both competent and trustworthy. As a first step check for FSCA (Financial Sector Conduct Authority) authorisation (and a list of products the advisor is approved to provide) here.

If worst comes to worst and you feel that your advisor has let you down and should refund you, the bottom line (in a nutshell) is that to successfully sue you will have to prove that you suffered loss in consequence of following your advisor's negligent advice.

The million dollar question (literally perhaps) is of course - how do you establish that necessary element of negligence? Whilst it will never be easy, and whilst each case will be treated on its own merits, the SCA (in the R11m case above) usefully held that an advisor's legal duties are mirrored in the FAIS (Financial Advisory and Intermediary Services) Act and its Codes of Conduct. So perhaps start off by proving a breach of the General Code of Conduct's provision that "an authorised financial service provider ‘must at all times render financial services honestly, fairly, with due skill, care diligence and in the interests of clients and the integrity of the financial services industry'."

There's also the FAIS Ombud option

You may not need to go to court to recover your losses, in that the "FAIS Ombud" (Ombudsman for Financial Services Providers) has the power to resolve complaints against FSPs. It can award "fair compensation for the financial prejudice or damage suffered" up to its jurisdictional limit of R800,000. In at least two Sharemax complaints, compensation orders have been issued, but many more have been dismissed.

Ask your lawyer which route is best for you.

And last but not least, some advice for financial advisors

Make sure that all your documentation protects you from liability as much as possible, that you have insurance cover in place in case you are sued (in the R2.5m case mentioned above, the insurers were ordered to indemnify the advisor against the claim), and that you comply strictly with FAIS and its Codes.