The AFCA Approach to misleading conduct

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We have created a series of AFCA Approach documents, such as this one, to help consumers and financial firms better understand how we reach decisions about key issues.

These documents explain the way we approach some common issues and complaint types that we see at AFCA. However, it is important to understand that each complaint that comes to us is unique, so this information is a guide only. No determination (decision) can be seen as a precedent for future cases, and no AFCA Approach document can cover everything you might want to know about key issues.

1 At a glance

1.1 Scope

AFCA and its predecessor schemes often receive complaints from complainants saying that a financial firm has misled them.

This document sets out our approach to assessing complaints about misleading conduct. The approach has been adopted from one of AFCA's predecessor schemes, the Financial Ombudsman Service.

1.2 Summary

Misleading conduct is conduct that leads, or is likely to lead, a person into error. It is prohibited by Australian law.

It can occur through statements, acts, omissions or silence, even if there is no intention to mislead.

When assessing complaints about misleading conduct, AFCA will:

- ask complainants and financial firms to supply relevant information
- consider all the available information to conclude what is most likely to have happened
- for complaints not within AFCA's superannuation jurisdiction we will do what, in our opinion, is fair in all the circumstances, bearing in mind legal principles[1].

If AFCA finds that a financial firm has engaged in misleading conduct, the remedy is not to necessarily make the misrepresentation come true. Rather, AFCA will compensate a complainant for any loss which they have suffered by relying on the misrepresentation[2]. AFCA may reduce the amount of any compensation if we believe a complainant did not take reasonable care to protect their own interests.

[1] For a superannuation complaint AFCA must apply a different decision making criteria. In a superannuation complaint we will decide whether the decision or related conduct of the superannuation provider was unfair or unreasonable in the circumstances. AFCA cannot make a decision that is contrary to the law.

[2] For a superannuation complaint AFCA may substitute its decision that compensation is payable in the circumstances for the purpose of removing any unfairness or unreasonableness arising from a decision of the superannuation provider not to compensate the complainant. The approach to assessing if the conduct was misleading and associated loss will be the same.

2 In detail

2.1 Understanding the general principles

What is misleading conduct?

Conduct is misleading when it leads, or is likely to lead, someone into error or to believe something that is false.

Misleading conduct can happen when a financial firm:

- says something that is wrong
- acts in a way that misleads a complainant
- does not say or do something when it should.

Misleading conduct can occur even if the financial firm did not mean to mislead or the complainant could have found out the true position by looking into the matter further.

However, if complainants do not take reasonable care to protect their own interests, AFCA might:

- find that a representation was not a 'real inducement' to enter into a contract or to pursue a particular course of action
- reduce the amount of compensation we award (see 2.4).

Which laws apply?

For financial services, section 12DA of the *Australian Securities and Investments Commission Act 2001* (ASIC Act) and section 1041H of the *Corporations Act 2001* both prohibit misleading conduct.

Section 12DA of the ASIC Act states:

> "A person must not, in trade or commerce, engage in conduct in relation to financial services that is misleading or deceptive or is likely to mislead or deceive."

2.2 Identifying types of misleading conduct

Can 'silence' be misleading?

In certain circumstances, a financial firm might mislead a customer by staying silent when it should say something.

Legally, bankers and lenders (unlike insurers) have no general duty of disclosure (although they are obliged to disclose some information under laws like the National Credit Code). For example, a lender is not usually required to draw a customer's attention to a particular term in a contract.

However, where in all the circumstances a customer has a reasonable expectation that the lender will disclose certain information, its failure to do so might be misleading conduct by silence.

Take loan break costs, for instance. If the customer asks the financial firm directly about the cost to break a fixed-rate loan but the financial firm remains silent or gives an incomplete response, the financial firm's conduct might be considered misleading and it might be liable to pay compensation.

There is also a reasonable expectation that relevant facts will be disclosed by:

- financial advisers in their advice processes.
- financial firms in their product disclosure statements for financial products.

What about predictions and opinions?

A prediction or opinion is not necessarily misleading if it turns out to be incorrect.

However, a person making a representation about a future matter, such as a profit or investment forecast, must have reasonable grounds for doing so and present evidence of these.

Without evidence, AFCA will assume the person did not have reasonable grounds to make the representation.

2.3 Assessing misleading conduct complaints

What information does AFCA need?

When assessing a misleading conduct complaint, AFCA looks at all the circumstances of the case. We consider two main questions:

1. did the financial firm mislead the complainant?
2. if so, did the complainant suffer a loss by relying on the financial firm's misleading conduct?

We usually request the following information:

Party	Information
Financial firm	A statement outlining the relevant officer's recollection of what was said. (If the officer no longer works for the financial firm, we expect the financial firm to make reasonable efforts to contact them for a statement.)
	A copy of any file notes recording conversations with the complainant.
Complainant	Any records made of the alleged representation or any written document containing the representation.

We will also look at the case's context. For example, if the misleading conduct relates to text in a brochure, we will review the whole brochure.

How do we reach a view in these complaints?

AFCA is not a court of law. We cannot take or test evidence on oath, or require third parties to give evidence. Instead we consider:

- available documents.
- the recollections of the parties.
- all relevant circumstances, including the complainant's conduct.

We give more weight to written records created when the alleged conduct took place because they are more likely to accurately reflect what was said.

If there are no records, we will decide what is most likely to have occurred based on the information we receive. If there are conflicting recollections and these are evenly weighted, we may find that a complainant's claim cannot be established.

2.4 Awarding compensation

What is the remedy for misleading conduct?

We may award compensation[3] when we find a complainant has suffered loss by relying on a financial firm's misrepresentation. To assess compensation, we consider how much worse off the complainant is. We compare the complainant's current position with their likely position had there been no misrepresentation.

Put another way, we ask complainants what they would have done differently. Was the expected benefit available elsewhere in the market? Did they lose the chance to gain that benefit?

When will AFCA not award compensation?

We will not award compensation if the complainant:

- cannot show that they relied on the misleading conduct and suffered loss
- as a result
- would have suffered the loss regardless of the misleading conduct
- would not have been able to gain the benefit or take up the opportunity elsewhere.

The available information must support the complainant's claim.

[3] Or in a superannuation context, decide that compensation is payable

What happens if the complainant has not acted reasonably?

AFCA may reduce the compensation if the complainant's loss was caused by both:

- the financial firm's misleading conduct, and
- the complainant's own failure to take reasonable care.

We will consider how much the complainant contributed to the loss.

However, if the financial firm acted fraudulently or with the intent to cause loss and damage, we will not reduce the complainant's compensation.

3 Context

3.1 Case studies

The case studies below are based on determinations by two of AFCA's predecessor schemes, the Financial Ombudsman Service and the Superannuation Complaints Tribunal (SCT). While previous determinations (by AFCA or by its predecessor schemes) are not binding precedents, where relevant they will inform AFCA's approach to an issue.

Case 1: Misrepresentation about property finance pre-approval

Over 12 years, the complainant, a property development company, had bought numerous properties at auction based on verbal funding pre-approval from an officer at the financial firm.

The complainant's directors said that the officer verbally pre-approved funding for another purchase at a meeting in 2009.

Believing that finance was unconditionally approved, the complainant then bought a property at auction. However, on the evening before settlement, the financial firm officer advised that finance had been declined. The sale contract had no 'subject to finance' clause.

The directors sought compensation for costs of $16,541.48 because of the financial firm's misleading conduct. The financial firm disputed that the officer had given pre-approval, but it could not supply notes from the meeting.

FOS found that:

- the financial firm officer had led the directors to believe that the financial firm had approved finance before the auction
- the directors had then relied on this representation to enter into the purchase contract

- the financial firm’s misleading conduct caused financial loss of $8,388.38 (see table), which it should compensate.

Consideration		Amount
Loss	Vendor fee for delaying settlement	$10,000
	Conveyancer fee for renegotiating and refinancing the purchase	$275
	Lost rental income from delayed settlement	$2,777
Benefit	Loan repayments the complainant avoided by not obtaining a loan before settlement	- $4,663.62
Total		$8,388.38

FOS did not support the directors’ claim for credit card interest costs. This was because they could have withdrawn from the purchase when the financial firm declined funding, avoiding these extra costs.

Case 2: Misleading conduct by silence over construction funds

The complainants applied to the financial firm for low doc loans to buy two blocks of land, which they intended to build on. The financial firm was aware of their plans at the time. However, when they later applied for finance to develop the blocks, the financial firm declined their application.

The financial firm’s loan file included a handwritten note to the lending officer saying it could not provide a low doc loan for construction. Its policy also stated that low doc loans were not available for property development. Yet the financial firm did not communicate this to the complainants when they applied for the original loans.

FOS found that the complainants had a reasonable expectation that the financial firm would disclose its inability to fund construction as it was aware they were:

- buying the blocks as investments and intended to build on them
- likely to need funds for future development.

By remaining silent, the financial firm misled the complainants and needed to compensate them.

This meant the financial firm should take possession of the blocks, pay the costs of selling them and keep the proceeds. The financial firm should then extinguish the complainants’ loans and:

- refund all repayments the complainants had made to the loans

- pay the complainants' costs for obtaining the loans and purchasing the blocks (including deposits, stamp duty and legal costs)
- pay their costs for owning the land (including council rates, water rates and pre-building costs)
- pay $4,000 for stress and inconvenience.

Case 3: Apportionment of loss for loan break costs

In 2008, the complainants took out a five-year fixed rate loan with the financial firm. The complainants paid out the loan about one year later with a break cost of $32,795.

They told FOS they had expected this break cost to be no more than $3,000 based on phone conversations they had with financial firm officers before entering into the loan contract.

FOS found it was more likely than not that the financial firm discussed a break fee of around $3,000 but did not tell the complainants that a break cost might also apply based on falling interest rates.

FOS took into account that the complainants clearly and consistently recalled the conversations, while the financial firm officers neither recalled nor recorded them.

FOS was satisfied that the complainants were misled, because any discussion about fees for ending a fixed rate contract early must be comprehensive. It must include both the known fees and the possibility that other fees might apply if interest rates fall.

However, FOS reduced the amount of compensation for the complainants by 70% because:

- the financial firm wrote to the complainants after their conversations to explain that a break cost might apply if the loan was prepaid and that it could not be calculated until it was actually prepaid
- the complainants did not clarify the letter with the financial firm, even though it went against what they had previously been told
- they had always planned to sell their property and break the loan after 12 months, so they should have fixed it for 12 months rather than five years.

FOS found the financial firm should repay the complainants 30% of the break cost paid – $9,838.70 – plus interest on this amount at the variable loan interest rate.

Case 4: Misrepresentation about policy coverage

The complainants were moving house and asked the financial firm about their contents insurance while they were in transit to their new address.

The financial firm's consultant told them they would be covered but did not say this was limited to two events: fire and motor vehicle accident.

When the complainants' contents were damaged by both rain and the removalists, the financial firm denied their claim because these were not insured events.

FOS found that the financial firm consultant's unqualified response was misleading by omission. The consultant should have told the complainants that the cover was limited or referred them to the policy document.

So it was reasonable that they assumed the same level of cover applied during the move as would have applied if the contents had been damaged at their home.

FOS also accepted the complainants relied on the misrepresentation given that they:

- asked the consultant a specific question
- were entitled to expect the consultant to be familiar with the policy
- were given an unqualified response.

The fact that the complainants had a copy of the policy did not help the financial firm given the specific misrepresentation occurred at almost the same time as the loss.

However, FOS only accepted the rain-damaged items as the complainants' loss because their contents policy did not include accidental damage or the actions of removalists.

Case 5: reliance on benefit estimate

The complainant disputed a superannuation trustee's decision to decline to compensate him for the difference between an estimate of the amount of his superannuation benefit given to him ($456,415) and the actual amount paid to him ($368,820).

The difference was due to the deduction of a surcharge debt and the application of negative earnings between the time of the estimate and the time of payment. The estimate disclosed that it was based on an assumed earnings rate of 4.5% and also warned that its accuracy could not be guaranteed because it was based on available information at the time.

The complainant could not show that he had relied on the estimate to his disadvantage; for example, by entering into a financial commitment based on the estimate or that he had suffered actual loss, other than his loss of expectation. The SCT therefore affirmed the trustee's decision as fair and reasonable in the circumstances because of both the trustee's disclaimer on the estimate and the lack of reliance and loss on the part of the complainant.

3.2 References

Definitions

Term	Definition
Complainant	individual or small business that has lodged a complaint with AFCA
AFCA	Australian Financial Complaints Authority
FOS	Financial Ombudsman Service
SCT	Superannuation Complaints Tribunal
Financial firm	a financial services provider that is a Member of AFCA
Superannuation provider	a superannuation trustee, RSA provider, approved deposit fund trustee or life company issuing a superannuation annuity

Useful documents

Document	Title / Link
Rules	www.afca.org.au/rules
Legislation	*Australian Securities and Investments Commission Act 2001* *Corporations Act 2001*