

The FOS Approach to Disputes lodged by guarantors

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

These documents explain the way we approach some common issues and dispute types that we see at FOS. However, it is important to understand that each dispute 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 FOS Approach document can cover everything you might want to know about key issues.

1 At a glance

1.1 Scope

A guarantor is a person or business who guarantees to pay back a loan if the borrower does not. We can consider most disputes lodged by guarantors who have guaranteed the debts of individual or small business borrowers. This document sets out the types of guarantor disputes we can consider, and outlines the things we take into account when considering whether the financial services provider fulfilled its obligations when it accepted the guarantee.

1.2 Summary

Who should read this document?

1. Financial services providers (FSPs) that obtain guarantees from individuals or small businesses.
2. Individuals or small business owners who have provided guarantees to FSPs.
3. Anyone required by an FSP to make payment on a guarantee (or likely to be pursued for payment) who does not consider they are liable for all or part of the amount being sought.
4. Anyone required by an FSP to make payment on a guarantee who thinks they will experience financial difficulty as a result of repaying the amount.
5. Anyone who wants to understand:
 - how FOS resolves disputes involving guarantees, and
 - how we decide whether we are able to consider disputes involving a guarantee.

Summary of the FOS Approach

We can review most disputes lodged by guarantors, as long as they fall within our [Terms of Reference](#)¹.

If the guarantor or borrower is a company, we can only consider the dispute if they are a “small business” as defined in our Terms of Reference.

If an FSP is not a subscriber to the Code of Banking Practice (CBP), we still expect them to generally follow the Code’s guidelines which relate to taking guarantees. This is because the Code generally represents good industry practice.

In some limited circumstances, a guarantor may lodge a dispute that would normally be brought by the borrower.

¹ Terms of Reference (<http://www.fos.org.au/tor>)

Guarantors can lodge a dispute at FOS if they are experiencing financial difficulty as a result of making payments under a guarantee.

2 In detail

2.1 The FOS Approach

Who can lodge a dispute at FOS involving a guarantee?

Our [Terms of Reference](#)² describe the types of disputes we can consider.

In most cases, we can consider a dispute between an FSP and a consumer about a guarantee or security that the consumer has given for the repayment of credit provided by the FSP to a borrower.

To be able to lodge a dispute with us that involves a small business, the business must fit the definition of 'small business' given in our Terms of Reference. This means that it must have had fewer than 20 employees (or fewer than 100 employees if the business involves the manufacture of goods) at the time of the act or omission that gave rise to the dispute.

So, we can consider a dispute about a guarantee that relates to a business loan for a small business, as long as the borrower is a small business as defined above. If the guarantor is also a company then it must also fit the small business definition.

If the dispute relates to a guarantee provided for a small business, a guarantor can lodge a dispute about the circumstances of entering the guarantee no matter what the solvency or registration status of the borrower is.

Monetary limits on a guarantor's claim

Our Terms of Reference state that we cannot consider a dispute if the consumer is claiming more than \$500,000, and the maximum compensation we can award is limited to \$309,000 per claim (plus interest, if appropriate).

We cannot set aside a portion of a guarantee. This means that if the guarantor is seeking to have a guarantee set aside, then the guaranteed debt must be less than \$309,000.

However, if an FSP is seeking to recover a final amount to extinguish the debt that is less than \$309,000, then we will generally be able to consider the dispute even though the full guarantee limit may be for more than \$309,000.

If the guarantor's dispute is about a request for financial difficulty assistance, we will consider the dispute regardless of the guarantee amount.

² Terms of Reference (<http://www.fos.org.au/tor>)

What is good industry practice for FSPs when obtaining a guarantee?

When we make decisions about disputes, we consider what is fair in all the circumstances, and take into account things like good industry practice and any applicable industry codes.

Even if an FSP is not a subscriber to the Code of Banking Practice, we still expect it to follow the Code's guidelines that relate to the taking of guarantees. This is because the Code represents good industry practice and generally reflects the FSP's common law obligations.

If we find that the FSP did not meet its obligations to the guarantor when it obtained the guarantee, we may decide that the FSP cannot rely on the guarantee.

We will look at whether the FSP:

- gave the guarantor sufficient notice about seeking independent legal and financial advice and about the financial risks involved in providing a guarantee
- gave the guarantor sufficient information about the borrower or credit facility
- gave the guarantor a copy of the related credit contract, letter of offer or other relevant information
- gave the guarantor sufficient time in which to consider the information relevant to the guarantee
- provided the guarantee to the guarantor or to a third party for signing, and if it was to a third party, whether that was appropriate
- ensured the guarantee was signed in an appropriate environment

Can a guarantor raise a claim on behalf of the borrower?

There might be times when a guarantor considers that they should not be liable for the full amount of the guarantee that the FSP is asking them to pay. This can happen where, for example, it is suggested that the FSP has sold the borrower's assets for less money than they were worth.

The borrower would usually bring this dispute, not the guarantor. However, if the borrower is not able to formally lodge the dispute themselves (for example, if they are bankrupt or in liquidation), then we may consider accepting the dispute from the guarantor if the FSP is asking them to repay the debt.

We will assess the circumstances of each dispute before we decide whether a guarantor can lodge a dispute to reduce the amount they have to pay by the amount of the borrower's claim. An example of when we would accept the dispute from the guarantor is if we thought it would be unfair for the FSP to recover a debt from the guarantor without taking the borrower's claim into account.

However, wherever possible, we consider that the borrower should lodge the dispute themselves if they are able to do so (ie they are not bankrupt or in liquidation).

If a guarantor lodges a dispute at FOS and the borrower has not, then the FSP is able to pursue the borrower for the debt even while the guarantor's dispute is open at FOS.

What if there are multiple guarantors?

If a guarantor lodges a dispute with FOS, the FSP cannot take action to recover the debt from the guarantor while the FOS dispute remains open. The FSP can, however, still try to recover the debt from the original borrower.

If there is more than one guarantor, the FSP may still take action to recover the debt from any guarantors who have not lodged a FOS dispute.

However, the FSP cannot take action against other guarantors to recover the debt if this action will affect any guarantors who have lodged FOS disputes. For example, if multiple guarantors own the same property over which the FSP has security for their liability, including the guarantor who lodged the dispute, the FSP cannot repossess the property because this action would affect the guarantor who had lodged the FOS dispute.

What if the guarantor is experiencing financial difficulty?

If a guarantor experiences financial difficulty as a result of repaying a guaranteed debt, they can lodge a dispute with FOS about their financial difficulty. We will consider these disputes regardless of the amount guaranteed.

If a guarantor acknowledges their liability but is having difficulty repaying it, we consider it is good industry practice for an FSP to give genuine consideration to the guarantor's financial difficulty.

Some options available to the FSP to provide financial difficulty assistance include arranging a 'time to pay' arrangement or an instalment arrangement.

If the parties cannot agree on a realistic repayment arrangement, the FSP should consider allowing a reasonable time for the guarantor to sell assets, or negotiate a timeframe for the guarantor to try to refinance the debts into their own name.

3 Context

3.1 Case studies

Case 1: Guarantee for a company's debts

A small business defaulted on its repayments. The FSP took possession of the company's assets and then sold them, which resulted in a shortfall of \$100,000. The company was then placed in liquidation and the FSP claimed the shortfall debt from the guarantor, Mr B.

Mr B had concerns about the way the FSP had sold the company's assets, and lodged a dispute at FOS.

Even though the company borrower was in liquidation, we decided that the guarantor was entitled to lodge a dispute alleging that the FSP had failed to comply with its duties as a mortgagee in possession when it sold the company's assets. We decided this because in the circumstances, it would have been unfair to allow the creditor to recover the debt under the guarantee without considering this part of the dispute.

After we asked the FSP to give us more information about the process it followed when it sold the company's assets, the FSP decided to abandon its claim against Mr B.

Case 2: Guarantor's remorse

Charlie's friend wanted a personal loan in order to purchase a popular restaurant and cafe in the city, and he asked Charlie to be a guarantor. Charlie obtained a copy of the relevant documents (including the proposed guarantee) from the FSP, and sought independent financial and legal advice. After a few days, Charlie signed the guarantee and provided the FSP with security over his home.

Charlie's friend's business failed after running up debts of \$250,000 and Charlie's guarantee was called on to cover his friend's debts.

Charlie regretted his decision to sign the guarantee and refused to acknowledge any liability. He lodged a dispute at FOS.

We found that the FSP had:

- given Charlie sufficient notice about seeking independent legal and financial advice and about the financial risks involved in providing a guarantee
- given Charlie sufficient information about the credit facility
- given Charlie a copy of the credit contract and guarantee, and
- given Charlie sufficient time in which to consider all the information relevant to the guarantee.

On this basis, we determined that Charlie was liable for the full amount of the guarantee. A guarantor is not able to avoid liability simply because they later regret the decision to sign the guarantee.

3.2 References

Definitions

Term	Definition
Borrower	A consumer who receives an amount of money from a lender, and is obligated to repay it.
FSP	Financial services provider, a business that has chosen FOS as its external dispute resolution scheme and provides a financial service
CBP	Code of Banking Practice
Consumer	An individual or small business owner who uses the services of a financial services provider.
Financial Difficulty	Financial services provider (a business that has chosen FOS as their external dispute resolution scheme)

Useful links

These sites provide useful information to help people experiencing financial difficulty:

Australian Securities and Investments Commission's [MoneySmart](#) website

- www.moneySMART.gov.au

Australian Bankers' Association '[Doing it tough](#)' website

- www.doingittough.info

[Financial Counselling Australia](#) website

- www.financialcounselingaustralia.org.au

The [Code of Banking Practice](#)

- <http://bit.ly/291ZkqN>

The [FOS website](#) contains more information about what we do, the types of disputes we can consider, and our dispute resolution processes.

- www.fos.org.au

We have published other documents that outline [the FOS Approach](#). You can see them all at

- www.fos.org.au/approach