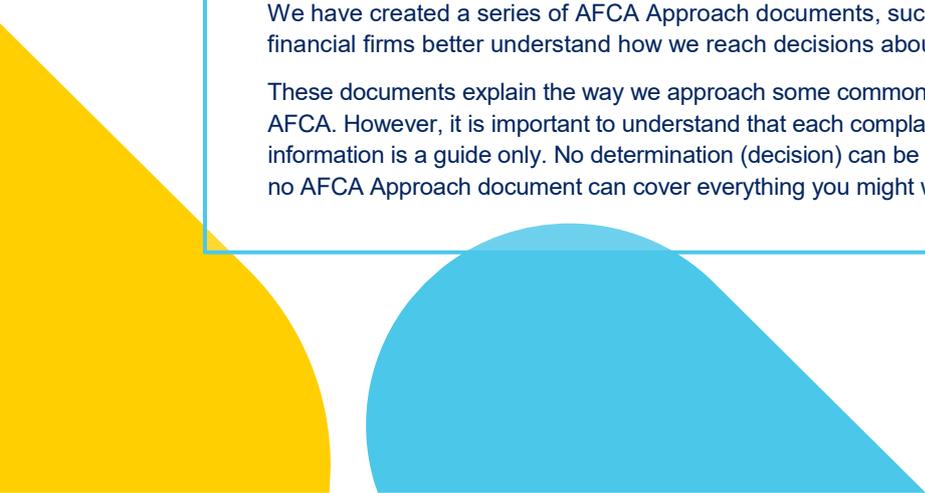


# The AFCA Approach to adequacy of statements of advice

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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 Purpose of this approach

## 1.1 Scope

The purpose of AFCA's approach documents is to explain the way we look at some common issues and complaint types. This approach outlines how we investigate and resolve disputes about the adequacy of Statements of Advice.

The *Corporations Act 2001 (Corporations Act)* generally requires financial firms to give a Statement of Advice<sup>1</sup> (SOA) to retail clients who receive personal financial advice. This is to ensure that retail clients are given enough information for them to understand the personal advice given to them and to decide whether or not to rely on it.<sup>2</sup> The statements and information in an SOA must be worded and presented in a 'clear, concise and effective' manner.<sup>3</sup>

AFCA and its predecessor schemes handle many financial advice complaints in which a retail client says they did not understand the advice they received from the financial firm. In these complaints, the quality and clarity of the information in the SOA is extremely important.

It is important to understand that each complaint that comes to us has a unique set of facts and this information is a guide only.

## 1.2 Summary

Financial firms are required to provide a SOA to retail clients who receive personal financial advice. The SOA is a key document in assessing whether adequate disclosure has been provided to retail clients, to enable them to understand the advice provided to them and rely upon it.

AFCA will analyse the SOA in all cases where this document has been provided to a retail client with a view to determining if the financial firm has complied with its obligations to the client under the *Corporations Act*.

## 1.3 Who should read this document?

- Financial firms that provide personal financial advice.
- Individuals who engage a financial firm to provide personal financial advice.
- Anyone who wants to understand how AFCA resolves complaints involving adequacy of statements of advice.

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<sup>1</sup> Section 946A of the *Corporations Act*. From 1 July 2013 financial firms must also comply with Section 961G of the *Corporations Act*

<sup>2</sup> ASIC *Regulatory Guide 175* at RG 175.167

<sup>3</sup> Subsections 947B(6) and 947C(6) of the *Corporations Act*

## 2 Jurisdiction

### 2.1 AFCA's purpose

AFCA is the independent external dispute resolution (**EDR**) scheme for the financial services sector. AFCA's purpose is to provide fair, independent and effective solutions for financial disputes. We do this by providing fair dispute resolution services. We also work with financial firms to improve their processes and standards of service to minimise future complaints. In addition to resolving financial complaints, AFCA identifies, resolves and reports on systemic issues and serious contraventions of the law.

### 2.2 AFCA's jurisdiction

AFCA can consider complaints against financial firms that are members of AFCA.

When a complaint is not resolved by agreement, negotiation or conciliation, we make a decision. Our decision reflects what is fair in all the circumstances having regard to legal principles, applicable industry codes or guidance, good industry practice and previous decisions of AFCA or predecessor schemes (which are not binding).<sup>4</sup>

When assessing conduct of a financial firm, we have regard to the law, codes, and standards of industry practice that were in place at the time of the conduct.

We may decide that a financial firm must compensate a consumer for direct financial loss, indirect financial loss or non-financial loss.<sup>5</sup> We may also decide that a financial firm is required to take, or refrain from taking, particular actions. If a consumer accepts our decision, the financial firm is bound by that decision.<sup>6</sup>

#### Fair in all the circumstances

Our decisions are intended to reflect what is fair in the circumstances of each complaint. This includes providing a fair outcome in cases where we find an error or breach has occurred.

In assessing what is fair, we apply a standard of fairness which focuses on concepts such as fair dealing, fair treatment and fair service. This allows us to assess the conduct of a financial firm over the life cycle of the firm's relationship with its customer.

The primary focus of our investigation is to assess whether the financial firm breached its obligations to the consumer. However, we also consider the conduct of the consumer when determining a fair outcome.

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<sup>4</sup> See AFCA Rule A.14.2.

<sup>5</sup> See AFCA Rule D.3.

<sup>6</sup> See AFCA Rule A.15.3.

## 3 In detail

### 3.1 How AFCA assesses the adequacy of SOAs in financial planning

#### The issue of informed consent

The question of whether a retail client has given their informed consent to take up the financial firm's advice is a critical issue in most financial advice complaints handled by AFCA.

Where this issue is raised, we will look at all of the disclosures made by the financial firm to the client. A key document is the SOA.

If the information in the SOA is not 'clear, concise and effective', then AFCA might find that the client did not understand the advice and the financial firm had failed to secure the client's informed consent to take up the advice.

#### What does 'clear, concise and effective' mean?

The phrase 'clear, concise and effective' is not defined in the Corporations Act. This means the words must be given their natural meaning.

According to the *Macquarie Concise Dictionary*:<sup>7</sup>

- 'clear' means 'free from obscurity ... confusion, uncertainty or doubt' and 'in plain language'
- 'concise' means 'brief and comprehensive; succinct; terse'
- 'effective' means 'producing the intended or expected result'.

When looking at whether information in an SOA is clear, concise and effective, we will consider whether the information:

- is expressed in plain language
- is brief yet comprehensive
- promotes understanding of the adviser's recommendations.

This approach is consistent with:

- ASIC's guidance in Regulatory Guide 175: Financial Product Advisers – Conduct and Disclosure<sup>8</sup>
- the Financial Planning Association's Code of Professional Practice.<sup>9</sup>

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<sup>7</sup> 3rd edition (2004), Macquarie Press

<sup>8</sup> June 2021 See paragraphs RG175.213 to RG175.217 (inclusive)

<sup>9</sup> See PS 4.4

### 3.2 What factors does AFCA consider?

When we consider whether or not a financial firm secured a client's informed consent to take up advice, we will examine the SOA provided to the client and consider the following questions:

#### 1. Did the financial firm consider the client's experience, language skills, literacy and numeracy?

Financial firms that make a reasonable assessment of a client's experience, language skills, literacy and numeracy are much more likely to prepare an SOA that the client will understand and less likely to be found to have breached their duty to secure the client's informed consent to take up the advice.

Remember, each client is unique.

#### 2. Did the SOA use language the client was likely to understand?

An SOA which does not use language the client is likely to understand cannot be effective.

It is important to note that the question is an objective one. In other words, we do not consider whether the client subjectively understood the information in the SOA. We only need to be satisfied that the client was likely to understand the language used in the SOA, assessed objectively, having regard to their experience, language skills, literacy and numeracy.

See the case study below for an example of how AFCA objectively assesses a client's understanding of an SOA.

#### 3. Did the SOA use legal, industry or technical language?

This question is closely related to question 2.

SOAs that use legal, industry or technical language are less likely to be 'clear, concise and effective' if the client is unfamiliar with this language. If the use of legal, industry or technical language in an SOA is unavoidable, the concepts must also be accurately explained in plain English.

#### 4. Was the information in the SOA in a logical sequence?

SOAs which are not logically set out are not clear or effective as they tend to confuse clients.

In broad terms, SOAs must have:

- a beginning – the client's objectives, available assets, timeframe and risk tolerance

- a middle – an analysis of strategies and/or products that are likely to meet the client’s objectives given their available assets, timeframe and risk tolerance
- an end – an explanation of a recommended strategy and/or products that are likely to achieve the client’s objectives given their available assets, timeframe and risk tolerance.

## **5. Did the SOA identify the client’s objectives in quantitative terms and explain how the advice would achieve those objectives?**

An SOA that identifies the client’s objectives in quantitative terms (e.g. ‘to retire at age 60 with sufficient savings to generate a retirement income of \$40,000 a year’) is much more likely to be effective than an SOA that does not identify the client’s objectives with such attention to detail (e.g. ‘to retire at age 60’).

The latter type of SOA is very unlikely to contain any meaningful analysis of, or conclusions about, the strategies and/or products that will achieve the client’s objectives.

## **6. Does the SOA resolve any internal conflicts?**

An SOA which is internally inconsistent is unlikely to be clear. If, for example, the client wants only a low level of risk but wants to retire with an income that may only be achieved by taking a greater risk the resolution of this conflict must be explained in the SOA. For example, the client may agree to take more risk, put more of their current income towards retirement or agree to the objective of retiring on a lesser income.

## **7. Did the SOA contain irrelevant information?**

Clients are likely to be confused by SOAs that contain irrelevant information.

For example, if a client has only sought advice about investment products, and does not wish to borrow to fund the proposed investment, the SOA need not include information about margin loans and insurance products. If the SOA includes this information, it is less likely to be clear, concise and effective.

## **8. Is the SOA a template document?**

In our experience, a template SOA is more likely to include:

- language the client will not understand (see question 2).
- legal, industry or technical language (see question 3).
- irrelevant information (see question 7).

Template documents can be helpful, but the financial firm must take care to tailor the language used in the template to the client and delete irrelevant information.

## 4 Application

The case studies below are based on determinations by AFCA.

### 4.1 Case studies

#### Case study 1 – Unclear and inappropriate financial advice (Case 683578)

The complainant is the corporate trustee of a Self-Managed Superannuation Fund (SMSF), represented by one of its directors, Ms D. Both Ms D and the complainant were clients of Mr G, a financial planner.

Mr G was an authorised representative of several Australian Financial Services Licensees during the client-adviser relationship but was only authorised by the financial firm between 29 January 2013 and 30 September 2016.

Ms D says she received inappropriate advice from Mr G to establish the SMSF, rollover her pre-existing defined benefit fund and purchase an investment property using a gearing strategy. The financial firm says the initial advice to establish the SMSF was provided before it authorised Mr G. It also says the investment strategy was driven by Ms D and she was fully aware of the risks of the SMSF's investment strategy.

The SOA indicated that the complainant's nominated objective was:

"I have an investment property in mind which I would like to know if I can buy it using my super".

However, the fact find's goal and objectives, scope of advice, risk profile and client declaration all remained blank. There was no evidence provided as to how the adviser reached the conclusion that the complainant's objective was as indicated. The decision maker was not satisfied that the information outlined in the SOA about the complainant's objective or risk profile reflected the complainant's actual circumstances at the time.

The financial firm was required to reimburse \$27,722.34 to the complainant's SMSF plus interest and contribute to the winding up costs of the SMSF.

#### Case study 2 – Unclear and inappropriate financial advice (Case 676803)

The complainant was an SMSF, represented by Mrs C as a director of its corporate trustee of the SMSF, and by Mrs C in her personal capacity.

Mrs C says, in 2014 and 2016, she was provided inappropriate financial advice from Mr G, an authorised representative of the financial firm, after being referred to the financial firm by Company T. Mr G's advice was to establish the SMSF and then have the SMSF invest in property.

The financial firm denies providing inappropriate advice in 2014 and says, if any liability is found, Company T should also be held liable for this advice. With respect to the 2016 advice, it says it cannot be held solely liable for the advice because Mr G was only authorised to provide advice under the financial firm’s license until 30 September 2016. From 1 October 2016 he was authorised to provide advice under a different AFSL.

The ombudsman found the financial firm was responsible for advice provided in June 2014 and December 2015. There was no evidence that Company T provided advice.

Mr G failed to identify the objectives, financial situation and needs of the client and did not conduct a reasonable investigation into the relevant financial products, fact find, and SOA were not completed.

It followed from that that Mr G did not have a reasonable basis to recommend a 70% Growth strategy and Mr G failed to properly advise on the risks of the strategy.

The adviser in this instance failed to collect valid data via a fact find, research, form recommendations based on the best interests, duty and formalise the recommendations via a SOA.

## 5 References

### 5.1 Definitions

Term	Definition
AFCA	Australian Financial Complaints Authority
Complainant	a person or small business who has lodged a complaint with AFCA
Financial firm	an organisation or individual who is a Member of AFCA
FOS	Financial Ombudsman Service
SOA	Statement of Advice

### 5.2 Useful links

Document type	Title / Link
<a href="#">Rules</a>	<a href="http://www.afca.org.au/rules">www.afca.org.au/rules</a>
Act	<i>Corporations Act</i> <a href="http://www.legislation.gov.au/Series/C2004A00818">www.legislation.gov.au/Series/C2004A00818</a>