



LICENSEE HEALTH CHECK: 6 SIMPLE QUESTIONS TO CHECK THAT YOUR REPRESENTATIVE AGREEMENTS ARE UP-TO-DATE

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A properly drafted representative agreement has the potential to save your business hundreds of thousands of dollars. However, a large number of financial services businesses are making do with basic, outdated and even poorly drafted agreements.

Whilst this article focuses on representative agreements between AFS licensees and their representatives, similar principles apply to representative agreements between corporate authorised representatives and their sub-authorised representatives.

Sections 917B and 917C of the *Corporations Act 2001* provide that AFS licensees are responsible for the conduct of their representatives, whether or not the conduct is within authority. The practical effects of this can be extremely onerous.

Whilst most representatives work honestly and diligently, there is a small number who, from time to time, engage in conduct which is negligent, dishonest and even fraudulent. Unfortunately, because AFS licensees are responsible for the conduct of their representatives, they are often targeted by ASIC and aggrieved clients.

When a representative gives unsuitable or inappropriate advice, it is not uncommon that they will give the same unsuitable or inappropriate advice to multiple clients. It is also not uncommon that, when the client complaints start to roll in, the representative will try and keep a low profile or leave to join another licensee, leaving the "old" licensee to try to pick up the pieces. There are even documented cases where the representative responsible for the problems with the clients (such as unsuitable or inappropriate advice) moves to a new licensee and tells the aggrieved clients that he will help the clients recover their losses from the "old" licensee.

We recently acted for a licensee where the representative's conduct resulted in more than \$12 million worth of claims against the licensee. The representative had a mental breakdown, and the licensee was left with multiple client complaints and a very angry regulator.

There is a common misconception that insurance cover alone will suffice. However, virtually all professional indemnity policies contain a number of exclusions. For example, most policies won't respond to conduct which was dishonest or fraudulent. Even where an insurance policy does respond, there is likely to be significant "deductibles" or "excesses".

An up-to-date representative agreement, drafted by lawyers with hands-on knowledge and experience with financial services, can be enormously effective.

When a licensee discovers that its representative has been negligent, dishonest or fraudulent, a well-drafted representative agreement will allow the licensee to:

- terminate the representative immediately;
- transfer the representative's clients to another adviser within the licensee group who is able to service those clients;
- restraint the former representative from soliciting the clients; and

- sue the former representative to recover any losses sustained by the licensee as a result of the former representative's conduct (including, without limitation, all legal fees, compensation payable to clients, fines and penalties and insurance deductibles).

Although some representatives may have sought to deliberately structure themselves as "men-of-straw", with key assets held by other persons or entities (such as in the names of spouses or other nominees) we typically find that most representatives have at least some assets in their own name. In addition, in many cases where we have sought to bankrupt former representatives in these circumstances (remembering that a bankrupt cannot act as a financial services representative, and as a consequence will lose control over their client registers and ongoing renewal and ongoing fees) it is surprising how often the representative can "find" the money to meet our claims on behalf of licensees.

We have acted for a number of licensees over the past decade where we have been able to successfully recover damages and indemnities from a wayward representative, which would not have been possible if the licensee did not have a well-drafted representative agreement.

Health check

If you are not confident answering any of the questions below, you may wish to have your contractual arrangements with your representatives reviewed by one of our solicitors.

1. Does your representative agreement state what the representative is permitted to do, and equally importantly, what the representative is prohibited from doing? Most financial services business have specific requirements as to what their representatives can and cannot do.
2. Does your representative agreement allow you to terminate the representative immediately in certain situations, e.g. where you reasonably believe the representative has failed to provide financial services efficiently, honestly and fairly?
3. Does your representative agreement state what happens once the representative has been terminated? For example, is the representative entitled to take their clients with them? Is the representative subject to a restraint?
4. Does your representative agreement contain an indemnity clause? In other words, if your representative's conduct results in financial claims against your licence, as a result of which you suffer losses, are you able to sue the representative to recover your losses?
5. Does your representative agreement properly describe how the representative is to be paid for their services? For example, when is the representative's remuneration calculated and paid? Are you allowed to set-off the representative's remuneration against amounts which the representative owes you?
6. Does your representative agreement meet the general requirements for a valid contract, including certainty and completeness. Representative agreements which are insufficiently certain or complete are unlikely to be upheld by a court.

We can perform a preliminary review of your existing representative agreement and, if we believe that you need a new or amended agreement, offer you very competitive rates.

FURTHER INFORMATION

For further information on any of these articles, please contact:

Mark Halsey
In-house Counsel - Licensee Solutions
T | (08) 9381 2914
E | mark.halsey@halseys.com.au

Kah Wai Hew
Senior Consultant
T | (08) 9381 6187
E | kah.wai@licenseesolutions.com.au

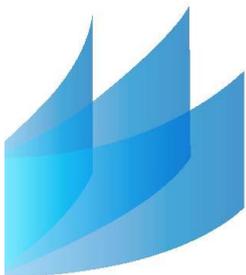
Fiona Halsey
Director - Halsey Legal Services
T | (08) 9381 2914
E | fiona.halsey@halseys.com.au

Kei Sukmadjaja
Solicitor
T | (08) 9381 2914
E | kei.sukmadjaja@halseys.com.au

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Everything for the AFS Licensee
(08) 9381 6187
www.licenseesolutions.com.au

45 Ventnor Avenue, West Perth WA 6005
PO Box 9046 Nicholson Road, Subiaco WA 6008
consultant@licenseesolutions.com.au

Halsey Legal Services
Barristers & Solicitors
(08) 9381 2914
www.halseys.com.au

45 Ventnor Avenue, West Perth WA 6005
PO Box 9046 Nicholson Road, Subiaco WA 6008
reception@halseys.com.au