benchtv
a benchmark production

Précis Paper

Liability of Australian Financial Services Licensees for the Misconduct of Their Authorised

Nicholas Kidd SC and Shahan Ahmed review sections of the *Corporations Act 2001* (Cth) governing the provision of financial services. They also review liability for misconduct by authorised representatives in the provision of such services with reference to *Casaclang v WealthSure Pty Ltd* [2015] FCA 761.

Discussion Includes

- The requirement under the *Corporations Act 2001* (Cth) that a person who provides financial services must hold an Australian Financial Services Licence ("AFSL")
- "Financial products" for the purposes of the Act
- Liability of holders of an AFSL for the misconduct of their authorised representatives and the different avenues under the Act for sheeting home liability
- What lessons can holders of an AFSL, and their lawyers, draw from *Casaclang v WealthSure Pty Ltd* [2015] FCA 761?

Précis Paper

Liability of Australian Financial Services Licensees for the Misconduct of Their Authorised

1. In this edition of BenchTV, Nicholas Kidd SC (Barrister) and Shahan Ahmed (Barrister) discuss the Federal Court of Australia's (Buchanan J) decision in *Casaclang v WealthSure Pty Ltd* [2015] FCA 761 which considered when Australian financial services licensees are liable for the misconduct of their authorised representatives. Mr Kidd SC led Mr Ahmad in acting for the successful applicants, Casaclang and others, in the Federal Court action.

Background

2. Colin Oberg was an accountant who between October 2004 and September 2010 was an authorised representative of Wealth Sure with authority to deal in specific classes of financial products including superannuation.

3. WealthSure was a financial services firm that was established in 2001 and operated out of Perth. Part 7.6 of the *Corporations Act 2001* (Cth) ("the Act") and specifically ss 911A & 911B require entities that carry out financial services to have an Australian Financial Services Licence (AFSL) or be an authorised representative of an AFSL licence holder. WealthSure had the relevant AFSL and Oberg provided financial services as a representative of WealthSure.

4. In the mid-2000s, Mr Oberg had a large number of 'mum and dad' clients with whom he had established substantial trust. In the period of 2008-2010, he advised them of an opportunity to invest money for a short time with no risk as part of a scheme he was involved in by providing money to him. The recommendation was usually made orally and occasionally in writing but with only limited details of the investment provided. A number of these 'mum and dad' investors provided money to Mr Oberg. Mr Ahmad reflects that the ease with which these investors provided their money is perhaps surprising. However, viewed within the context of Mr Oberg providing advice to these individuals for sometimes 20 years and to a reasonably high standard, it becomes more understandable.

5. From around 2010, WealthSure started to receive complaints from clients of Mr Oberg. On 20 September 2010 WealthSure suspended his authorised representative status and terminated it on 30 September 2010. What immediately ensued was notable in grounding WealthSure's liability. The licensee notified ASIC, as it was required to, but made no attempt to notify clients about the actions of Mr Oberg until 10 months later. Even then, they only attempted to contact some of his clients with a short letter that made no mention of his termination due to misconduct.

6. Ultimately, the money provided to Mr Oberg was never returned. What later transpired was that Mr Oberg not only used money provided to him by clients but also used money from accounts which he had access to without any form of permission.

7. Mr Oberg was permanently banned from providing financial services by ASIC and criminal charges were laid against him.

Federal Court Action - *Casaclang v WealthSure Pty Ltd* [2015] FCA 761

8. The case in the Federal Court was initially brought on the behalf of around 30 applicants who had lost almost the entirety of the money they had provided to Mr Oberg. Importantly, the only defendant to these proceedings was the licensee, WealthSure, and not Mr Oberg in his personal capacity. The applicants claimed damages from WealthSure for losses caused by the conduct of a previously "authorised representative" of WealthSure – what the presenters refer to as "sheeting home" liability to WealthSure.

Was Mr Oberg liable to the applicants?

9. Before considering WealthSure's liability to the applicants, his Honour, Buchanan J, first considered Mr Oberg's liability to the applicants. Ultimately, the court found that Mr Oberg had been liable to his former clients on 3 bases. Firstly, it was found that Mr Oberg owed a common law duty of care in negligence, which he breached causing his client's loss. Secondly, he owed a concurrent contractual duty of care which he also breached causing them loss. Finally, Mr Oberg was found to have contravened provisions of Part 7.10 of the Act, including s 1041E which prohibits a person from knowingly or recklessly making false or misleading statements likely to induce persons to apply for a financial product. The section provides:

SECTION 1041E:

False or misleading statements

(1) A person must not (whether in this jurisdiction or elsewhere) make a statement, or disseminate information, if:

(a) the statement or information is false in a material particular or is materially misleading; and

(b) the statement or information is likely:

(i) to induce persons in this jurisdiction to apply for financial products; or

(ii) to induce persons in this jurisdiction to dispose of or acquire financial products; or

(iii) to have the effect of increasing, reducing, maintaining or stabilising the price for trading in financial products on a financial market operated in this jurisdiction; and

(c) when the person makes the statement, or disseminates the information:

(i) the person does not care whether the statement or information is true or false; or

(ii) the person knows, or ought reasonably to have known, that the statement or information is false in a material particular or is materially misleading.

10. In order to ground liability under s 1041E it was necessary that the applicant show that the relevant arrangements were a "financial product" for the purposes of Chapter 7 of the Act. Relevantly, in the "labyrinthine provisions" of Chapter 7 (at [232] of *Casaclang*) there exists a general definition, specific exclusions and specific inclusions of the term. The applicants contended that the arrangements amounted to a financial product under the general definition in s 763A:

SECT 763A:

General definition of financial product

*(1) For the purposes of this Chapter, a **financial product** is a facility through which, or through the acquisition of which, a person does one or more of the following:*

(a) makes a financial investment (see section 763B)…

" A financial investment" is defined under s 763B:

SECT 763B:

When a person makes a financial investment

*For the purposes of this Chapter, a person (the **investor) makes a financial investment** if:*

*(a) the investor gives money or money's worth (the **contribution**) to another person and any of the following apply:*

(i) the other person uses the contribution to generate a financial return, or other benefit, for the investor;

(ii) the investor intends that the other person will use the contribution to generate a financial return, or other benefit, for the investor (even if no return or benefit is in fact generated);

(iii) the other person intends that the contribution will be used to generate a financial return, or other benefit, for the investor (even if no return or benefit is in fact generated); and

(b) the investor has no day-to-day control over the use of the contribution to generate the return or benefit.

11. On the facts, there was little dispute that the applicants had provided money to Mr Oberg and that they had no day-to-day control of the use of the funds. However, WealthSure contended that the applicants had in fact given Mr Oberg a loan which he promised to repay with interest and the applicants did not contend that Mr Oberg would use the money to generate a return for them. That contention was based on some evidence in which the arrangements were described as a loan and other parts of the evidence which suggested that Mr Oberg would repay the monies. However, his Honour was satisfied that the arrangements were not mere loans and that they were a "financial product".

12. Accordingly, Mr Oberg was liable to compensate the applicants under s 1041I.

Was WealthSure liable to the applicants for Mr Oberg's actions?

13. The next question for determination by Buchanan J was whether the liability of the authorised representative could be "sheeted home" to the AFSL licence holder. The applicant contended that there were six grounds on which the licence holder was liable for the authorised representative's misconduct.

14. The first ground flowed from Division 6 in Part 7.6 of the Act. The division specifically considers the attribution of liability of authorised representatives to licensees. It contains a low threshold for the division to apply. In particular, s 917A provides:

> **SECTION 917A:**
> ***Application of Division***
>
> ...
>
> *(2) This Division applies to any conduct of a representative of a financial services licensee:*
>
> *(a) that relates to the provision of a financial service; and*
>
> *(b) on which a third person (the **client**) could reasonably be expected to rely; and*
>
> *(c) on which the client in fact relied in good faith.*

The connection of "relates to" is very broad. However, the requirement that the conduct relate to a "financial service" again necessitates an examination of the definition of that term. As explained above, the arrangements were found to have been a "financial service" for the purpose of the Act.

15. The operative provision of the Division is found in 917B which provides:

SECTION 917B:

Responsibility if representative of only one licensee

If the representative is the representative of only one financial services licensee, the licensee is responsible, as between the licensee and the client, for the conduct of the representative, whether or not the representative's conduct is within authority.

This was an important advantage for the former clients because once the Division applies under s 917A it does not matter whether the conduct of the representative was "within authority". In [204]-[205], Buchanan J concluded that notwithstanding that Mr Oberg engaged in an enterprise of which WealthSure neither knew or would have approved, i.e. a "frolic of his own", s 917B makes WealthSure responsible.

16. Furthermore, s 917F provides further benefits to clients as follows:

SECTION 917F:

Effect of Division

(1) If a financial services licensee is responsible for the conduct of their representative under this Division, the client has the same remedies against the licensee that the client has against the representative.

(2) The licensee and the representative (along with any other licensees who are also responsible) are all jointly and severally liable to the client in respect of those remedies.

Subsection 2 effectively denies the application of proportionate liability to any claim against a licensee once Division 6 is engaged. Hence, WealthSure is entirely 'on the hook' for the applicants' losses,

17. WealthSure did contend that Division 6 did not provide any statutory remedies under the *Corporations Act* pursuant to s 917F(3):

SECTION 917F:

Effect of Division

…

(3) However, nothing in this Division imposes:

(a) any criminal responsibility; or

(b) any civil liability under a provision of this Act apart from this Division;

on a financial services licensee that would not otherwise be imposed on the licensee.

It was argued that Division 6 can only operate in respect of the liability of Mr Oberg under the general law or some other statute apart from the *Corporations Act*. The judge rejected this argument, stating that the purpose of s 917F(3) was merely to ensure that civil liability imposed elsewhere in the Act is not extended or added to by the operation of Division 6. For example, where a representative is liable under some other Division of the *Corporations Act*, Division 6 would operate to make the licensee liable to the same extent as the representative and no more.

18. It was also contended by WealthSure, that it is plain from the language of the Division that it ceases to apply where the authorised representative is no longer an authorised representative in fact. This was relevant because some of the losses were caused by conduct of Mr Oberg which occurred after his authorised representative status was revoked. It was purported that during these times liability could not be "sheeted home" to the licensee. This was accepted by the court.

19. The second ground on which liability was alleged to accrue to the licensee was via s 769B of the Act. The section does not specifically focus on the sheeting home of liability to a licensee from a representative although it provides:

SECTION 769B:

People are generally responsible for the conduct of their agents, employees etc.

(1) Subject to subsections (7) and (8), conduct engaged in on behalf of a body corporate:

(a) by a director, employee or agent of the body, within the scope of the person's actual or apparent authority; or

(b) by any other person at the direction or with the consent or agreement (whether express or implied) of a director, employee or agent of the body, where the giving of the direction, consent or agreement is within the scope of the actual or apparent authority of the director, employee or agent;

is taken, for the purposes of a provision of this Chapter, or a proceeding under this Chapter, to have been engaged in also by the body corporate.

Therefore, this section acts as a statutory vicarious liability deeming provision where (1) the conduct is "engaged in on behalf of" the licensee, and (2) is "within the scope of the person's actual or apparent authority". Although these two requirement must be met, the provision may continue to apply where actual authority is revoked but apparent authority remains, unlike Division 6.

20. According to the principles of actual and apparent authority emerging from *Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480, the relevant conduct of Mr Oberg was within his apparent authority. That finding was based on evidence that within

WealthSure's published documents the relationship between the licensee and its authorised representatives was described in broad terms. Furthermore, Mr Oberg's apparent authority continued until after the actual authority was suspended because no steps were taken to inform the applicants that Mr Oberg lacked representative status despite WealthSure knowing of Mr Oberg's conduct in relation to other client's funds. Effectively, s 769B operated as a second, alternative link to make WealthSure liable for Mr Oberg's breaches of s 1041E and his tortious and contractual duties of care.

21. The third link discussed involved s 79 of the Act. The provision defines when a person is "involved" in the contravention of the Act as follows:

SECTION 79:

Involvement in contraventions

A person is involved in a contravention if, and only if, the person:

- *(a) has aided, abetted, counselled or procured the contravention; or*
- *(b) has induced, whether by threats or promises or otherwise, the contravention; or*
- *(c) has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to, the contravention; or*
- *(d) has conspired with others to effect the contravention.*

Section 1041I provides:

SECTION 1041I:

Civil action for loss or damage for contravention of sections 1041E to 1041H

(1) A person who suffers loss or damage by conduct of another person that was engaged in in contravention of section 1041E, 1041F, 1041G or 1041H may recover the amount of the loss or damage by action against that other person or against any person involved in the contravention, whether or not that other person or any person involved in the contravention has been convicted of an offence in respect of the contravention.

(Emphasis added)

However, the High Court in *Yorke v Lucas* [1985] 158 CLR 661 determined that to be "involved" in a contravention required "actual knowledge" of the matters that constituted the contravention. Given the evidence showed that WealthSure had limited knowledge of the contraventions when they occurred, the applicant was unsuccessful in using ss 79 and 1041I to "sheet home" liability to the licensee.

22. The fourth route through which the applicant attempted to "sheet home" liability was pursuant to Part 7.7 of the Act. When "personal financial advice" is provided by an authorised representative "in their capacity" as an authorised representative to a "retail client" then it can only be provided where there is a reasonable basis for doing so. Section 953B makes WealthSure liable for any contravention of this provision. The definitions of "personal financial advice" and "retail client" are defined in ss 766B and 761G (not extracted), respectively:

SECTION 766B:

Meaning of financial product advice

(3) For the purposes of this Chapter, personal advice is financial product advice that is given or directed to a person (including by electronic means) in circumstances where:

(a) the provider of the advice has considered one or more of the person's objectives, financial situation and needs (otherwise than for the purposes of compliance with the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 or with regulations, or AML/CTF Rules, under that Act); or

(b) a reasonable person might expect the provider to have considered one or more of those matters.

Buchanan J determined the applicants had received "personal advice" and that they were indeed "retail clients". It was further necessary that the representative was "acting in their capacity" as an authorised representative. Unlike Division 6, where a representative is acting "on a frolic of his own", Part 7.7 will not "sheet home" liability to a licensee. The practical effect of this distinction was that the applicants had to be investing in a WealthSure approved product. In this particular case, some of the applicants were able to establish that they had indeed invested in such a product whilst others were not. Also discussed in Part 7.7 is the requirement that representatives provide a Statement of Advice ("SOA") under s 946A. His Honour found that there were no SOAs provided by Mr Oberg. Again, only those successful in showing that they had invested in a WealthSure approved product were able to establish this contravention.

23. The fifth route considered provisions under Part 7.9 of the Act. Section 1021A sets out the situations in which a product disclosure statement ("PDS") is required to be given. Section 1013D sets out the main requirements of what should be given in such a disclosure. It is an offence under the Act to not provide a suitable disclosure where required. In order to ground liability under this Part, it was necessary for the applicants to show that they would not have continued with the proposed investment opportunity if they were provided with a valid PDS. WealthSure were made liable pursuant to s 1022B.

24. The sixth and final route was contended to be WealthSure's direct liability arising in negligence. Mr Oberg had been found to owe a duty of care, that he breached that duty and caused the applicants' loss. It was further alleged that WealthSure owed a duty to the applicants to take reasonable steps to warn them that his authority had been revoked following its termination. His honour, Buchanan J, found such a duty existed and that WealthSure's actions were insufficient in this regard, breaching the direct duty they owed in negligence to the applicants.

Implications

25. In light of the decision in *Casaclang*, it appears that financial services licensees should have far more regular and comprehensive monitoring and auditing of their authorised representatives. Furthermore, steps needs to be taken in the period following the termination of an authorised representative's appointment to ensure that they do not manifest apparent authority. This may include physical attendance at the office of the former representative to ensure there are no clear vestiges of apparent authority including stationery from the licensee.

26. Finally, Buchanan J at [236] remarked upon the inadequacies of Chapter 7 for the purposes of determining the relevant standard of conduct for those operating under an AFSL:

> The standards of conduct which are set out in the *Corporations Act* in general and in Chapter 7 in particular should operate as a reliable guide to conduct, readily ascertainable and capable of equally ready understanding. They should be accessible and comprehensible by those whose conduct is governed and by those whose interests might be affected – i.e. consumers and clients, small as well as big. The provisions with which I am dealing in this judgment fall short of that objective by a large margin, even for trained lawyers. That is unfortunate. The result is that the provisions of Chapter 7 do not, in my view, act as an effective guide to conduct at all. They represent a complicated catalogue from which to select instruments of retribution well after loss or damage has been suffered. The applicants in the present case have persevered, but justice for them and others (and for licensees) should not depend upon such complexities as Chapter 7 presents, and should not be endangered by the real possibility of misunderstanding or misapplication of its provisions.

It is be hoped that some form of amendment might clarify the operation of this division. However, the judgment of Buchanan J does provide some further guidance.

BIOGRAPHY

Nicholas Kidd SC

Barrister, Seven Wentworth Selborne Chambers, Sydney

Nicholas Kidd SC was admitted as a Lawyer in 1991. He was called to the NSW Bar in 1998 and appointed Senior Counsel in 2012. Nicholas practises in a wide range of matters with a focus on commercial and equity litigation. He appears in a variety of courts at trial and appellate level, as well as in tribunals, commercial arbitration hearings and mediations.

Shahan Ahmed

Barrister, Blackstone Chambers, Sydney

Shahan Ahmed was admitted as a Lawyer in 1998 and called to the NSW Bar in 2008. He is currently on the panel of barristers for a number of insurers for general insurance and product liability matters. He is also on the panel for the NSW Government's Building Insurers' Guarantee Corporation for building insurance cases. His overall practice is in building and construction, commercial, contracts, corporate law, equity, insolvency and property.

BIBLIOGRAPHY

Focus Case

Casaclang v WealthSure Pty Ltd [2015] FCA 761

Benchmark Link

https://benchmarkinc.com.au/benchmark/composite/benchmark_29-07-2015_insurance_banking_construction_government.pdf

Judgment Link

http://www.austlii.edu.au/au/cases/cth/FCA/2015/761.html

Cases

Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd [1964] 2 QB 480
Yorke v Lucas [1985] 158 CLR 661

Legislation

Corporations Act 2001 (Cth)