

The AFCA Approach to terms of settlement

November 2021

1	At a glance	2
1.1	Scope.....	2
1.2	Summary	2
2	In detail	4
2.1	Drafting terms of settlement.....	4
2.2	Understanding our governing principles.....	5
2.3	Understanding the effect of a terms of settlement	7
2.4	What happens if the terms of settlement are not complied with?.....	8
2.5	Making third party settlements.....	9
2.6	When will AFCA consider a complaint notwithstanding previous terms of settlement?	10
3	Context	13
3.1	Case studies.....	13
3.2	References	14

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

Central to AFCA's key purpose and values is to provide fair, balanced and independent decision making in disputes between financial firms and consumers. AFCA seeks to resolve complaints between a complainant and a financial firm in a cooperative, efficient, timely and fair way. The concept of what is "fair" extends to both how complaints are resolved and on what terms.

Whilst many complaints resolved at AFCA do not require any formal terms of settlement to be entered into, our Rules contemplate that there may be circumstances where the parties wish to formally record the resolution in writing. This may be referred to by various names including terms of settlement, settlement agreement, Deed, or Release. Deeds of forbearance can also contain settlement provisions, but this approach document does not deal with deeds of forbearance which involve some different considerations.

This document sets out our approach to settlement documents and to interpreting terms of settlement by outlining:

- What governing principles should inform the terms of settlement
- What the terms of settlement should cover
- What to consider when drafting non-standard terms
- How terms of settlement can affect a further or current complaint with AFCA.

This approach will help the parties to accurately document the resolution of a complaint and in particular provide guidance to

- the complainant before signing the terms of settlement
- the financial firm when drafting any terms of settlement.

It should be noted that AFCA is required by section 1052E of the Corporations Act and ASIC Regulatory Guide 267 to report concerns about any terms of settlement that it thinks may require investigation to the relevant regulator.

1.2 Summary

It is important when finalising a complaint at AFCA that any terms of settlement are a clear and accurate record of the agreement between the complainant and the financial firm. The purpose is to provide finality as to the subject matter of the complaint and certainty about the terms of the settlement reached. This helps to ensure there will be no further complaints about the content of those terms.

AFCA expects terms of settlement prepared by a financial firm to:

- be drafted fairly with a clear scope, usually in line with one of our standard templates
- follow our core guiding principles to protect each party's rights
- clearly explain the way in which the resolution will be given effect
- clearly set out the consequences of any breach or default under the terms of settlement
- where relevant, cover the financial firm's right to enter judgment on default or to restore legal proceedings, if the complainant breaches the terms.

If the complaint has been the subject of a binding determination by an AFCA Decision Maker under our general jurisdiction, terms of settlement must be provided (if at all) within the time allowed by AFCA, and be:

- limited to the matters dealt with in the determination
- consistent with the determination.

In some complaints, we will also consider previous terms of settlement that the financial firm and complainant have agreed.

Superannuation

Under our superannuation jurisdiction, a binding determination by an AFCA Decision Maker has immediate effect. Terms of settlement for our superannuation jurisdiction are therefore relevant only for a negotiated outcome, including if the parties agree to accept AFCA's preliminary assessment.

2 In detail

2.1 Drafting terms of settlement

Who supplies the terms of settlement?

If the financial firm asks the complainant to agree to terms of settlement following a preliminary assessment (for all jurisdictions) or determination (in our general jurisdiction), it will have to prepare the document and cover the costs for this. The complainant should get legal advice on any non-standard terms of settlement. We may ask the financial firm to pay the complainant's reasonable costs for this.

However, AFCA may record the terms of any settlement reached in an AFCA telephone conciliation conference and provide it to the parties.

Does AFCA check the financial firm's terms of settlement?

We do not give the complainant legal advice on the effect of the financial firm's terms of settlement. However, we can review the terms of settlement to ensure they are consistent with the outcome of the complaint and the principles governing AFCA.

If the terms of settlement do not adequately capture the settlement terms or exceed the agreement entered by the parties, we will ask the financial firm to redraft it to ensure it is consistent with the outcome of the complaint, and with AFCA's governing principles.

If we consider the settlement terms may require investigation, we may provide details of the settlement to the relevant regulator under section 1052E Corporations Act and ASIC Regulatory Guide 267, paragraphs 267.60-267.64.

We may find the terms of settlement are not fair and/or require investigation where:

- the scope is unreasonably wide, especially where the financial firm seeks to be released from being liable for its conduct beyond the scope of what was raised in the complaint or in settlement negotiations
- it does not reflect the preliminary assessment, determination or complaint resolution agreement that resolved the complaint
- it does not follow AFCA's governing principles (set out in Rule A.2.1)
- it prevents the complainant from referring a complaint to the relevant regulator(s)
- it is not a genuine and voluntary agreement (for example, the complainant entered it as a result of duress, misrepresentations, or unconscionable conduct)
- the settlement is manifestly disproportionate to the financial firm's liability and to the financial firm's and/or AFCA's approach to similar complaints.

2.2 Understanding our governing principles

What should the terms of settlement cover?

The following governing principles should inform the terms of settlement:

- 1 The terms of settlement should finalise the complaint.
- 2 They should reflect the agreement between the financial firm and the complainant, and not introduce new terms.
- 3 They should clearly outline the steps the parties are required to take to action the resolution.
- 4 They should expressly deal with the consequences of not complying with them. This should not allow the financial firm to try to recover:
 - > more than the agreed full debt plus recovery costs (this applies in circumstances where the debt is not disputed, and the agreement is limited to repayment terms, which if breached require the full debt to be paid), or
 - > more than the agreed compromised amount plus recovery costs.
- 5 A financial firm should use plain English when drafting its own terms of settlement.

How should the terms of settlement deal with breach or default by the complainant

Some complaints are settled on terms which leave the complainant with obligations (for example, complaints about credit contracts). The terms of settlement should clearly outline the consequences of a breach of, or default in, any such obligations. The terms of settlement should follow these principles:

- 1 The terms of settlement should generally give the complainant 7 days' notice to remedy a default before the financial firm is permitted to take action. If the action to be taken by the financial firm is to reinstate legal proceedings, the notice should state that the financial firm may obtain judgment by default unless the complainant corrects the default or files a defence with the court.
- 2 They should not prevent the complainant from disputing whether either party complied with the terms of settlement.
- 3 They may allow discontinued legal proceedings to be restored or reinstated on default. If so, the proceedings might need amending to reflect that a settlement agreement was not met.
- 4 They should not require the complainant to consent to judgment.

How should the terms of settlement deal with breach or default by the financial firm

Generally, if a financial firm breaches terms of settlement with a complainant, the complainant can submit a fresh complaint to AFCA about the financial firm's breach.

Where the parties agreed to resolve the complaint on the understanding the financial firm will do something (for example, pay the complainant compensation) and the financial firm fails to do so, the complainant would normally be to enforce the terms of settlement or to claim compensation for the loss caused by the financial firm's breach.

However, the terms can specify that in the event of breach, the complainant can treat the settlement as at an end and pursue the claims raised in the original AFCA complaint.

The terms of settlement should make it clear what rights the complainant has if the financial firm breaches particular terms in the agreement. The implications of this are explained in more detail in section 2.3.

Are there special requirements for settlements arising from an AFCA determination?

A determination is AFCA's final decision on the merits of a complaint. It will take effect or become binding as set out in Rule A.15.

Rule A.15.3 allows a financial firm to ask the complainant to sign a settlement agreement or release from liability as a condition of the firm complying with a determination, provided:

- The complaint is not a superannuation complaint. AFCA's determination of a superannuation complaint has immediate effect by law.
- The agreement:
 - > meets AFCA's requirements under the Rules and this Approach
 - > is provided to the complainant within the time specified by AFCA if any, either in the determination or otherwise, or within a reasonable time
 - > is limited to the matters dealt with in the determination
 - > is consistent with the determination, and with the parties' rights and obligations under the Rules.
- Any release of the financial firm from liability may only take effect after the financial firm fulfils all its obligations under the determination.

2.3 Understanding the effect of a terms of settlement

How is the settlement documented?

AFCA expects that when the complainant and the financial firm agree to resolve a complaint, it means the complaint will end. Documenting the terms of settlement is not a chance for either party to then change a mutually agreed resolution.

Generally, the terms of settlement:

- are binding
- should clearly set out the consequences of a breach or non-compliance with any of its terms
- effectively replace all previous contracts and arrangements to do with the complaint.

The usual remedy if terms of settlement are breached is to sue the party for breaching it.¹ However, this will depend on how the agreement is expressed.

The common types of compromises are either of the following:

- the complainant promises to abandon the claims raised in their complaint in return for the financial firm *doing* something (for example, paying compensation to the complainant or accept a lesser amount for a disputed debt under a loan contract)
- the complainant promises to abandon their claims in exchange for the financial firm *promising* to do something.

The distinction and the effect on the complaint being settled is important if the financial firm fails to do what is required.

With the first type of compromise, if the financial firm fails to perform what they said they would the complainant's original rights continue and can be enforced. This means they can submit a new AFCA complaint raising the same claims as the original complaint.

With the second type, the complainant has waived their original rights and can only enforce the terms of settlement and cannot lodge a new complaint raising the same claims as in the original complaint. They can only lodge an AFCA complaint claiming the financial firm breached the terms of the settlement agreement.

Therefore, it is important for the terms of settlement to detail what is the consequence of either party failing to perform what it said it would do under the agreement.

What if the complainant disputes the debt?

Where the complaint is about a credit contract, a complainant who disputes liability will often agree to resolve the complaint in exchange for paying the financial firm a

¹ See *McDermott v Black* (1940) 63 CLR 161, *Osborn and Bernotti v McDermott* [1998] 3 VR 1, and *Masters v Cameron* (1954) 91 CLR 353

smaller sum (“settlement sum”), rather than the sum owed under the disputed contract.

Where this occurs and the complainant does not make the required payments of the settlement sum, the financial firm should only take action to recover the settlement sum (plus recovery costs). This should be clearly set out in the terms of settlement.

Courts have held that in circumstances where a debt is disputed and a settlement sum is subsequently agreed, being a reduced amount of the sum due under the disputed contract, the financial firm is unable to take action other than for the settlement sum because:

- the original, larger sum owing was not an accepted debt
- the complainant gave up rights in exchange for the financial firm agreeing to a smaller sum being paid.²

What if the complainant does not dispute the debt?

By contrast, the complainant may not dispute the debt, but instead seeks a revised payment plan or payment of a reduced sum. This often arises if the complainant faces financial difficulty in paying the undisputed debt.

In these complaints the terms of settlement can require the complainant to pay the full debt (not just the smaller sum) if they default on the agreed settlement payments. If the terms of settlement do not specify a sum to be paid on default, the complainant must generally pay the full undisputed debt.

Can the parties agree that terms of settlement can be cancelled?

The financial firm and the complainant can agree that the terms of settlement will not stay in place unless the complainant meets their obligations. This usually depends on the complainant making payments in line with the settlement terms. If this is the intention of the parties, then this should be clearly set out in the terms of settlement.

2.4 What happens if the terms of settlement are not complied with?

How can the financial firm pursue court action if the complainant defaults under the terms of settlement?

If a complainant does not comply with the terms of settlement, the terms of settlement may provide that the financial firm can take legal action including proceeding to apply for judgment against the complainant.

² For more on this, see *Zenith Engineering Pty Ltd v Queensland Crane & Machinery Pty Ltd* [2000] QCA 221, and *Duffy Bros Fruit Market (Campbelltown) Pty Ltd v Gumland Property Holdings Pty Ltd* [2007] NSWCA 7.

But the terms of settlement should not require the complainant to agree or consent to judgment in these circumstances. The complainant is entitled to dispute the default under the terms of settlement should they wish to do so.

The terms of settlement should generally provide that a financial firm will give the complainant at least 7 days' notice of a default on the terms of settlement before legal or other enforcement action is able to be taken.

Can the financial firm re-start legal proceedings after settlement?

Sometimes, a complaint is brought in circumstances where legal proceedings that have been issued but not yet determined. Under our Rules, the financial firm must not pursue those proceedings while the complaint is open with AFCA.

Where legal proceedings have been discontinued and the complaint settled, but the complainant has then not complied with the terms of settlement, the financial firm can seek to restore or reinstate those earlier proceedings.

However, the terms of settlement must include the financial firm's right to do this. We consider this acceptable because it saves in court costs that the complainant would ultimately need to pay if the proceedings have to be reissued.

But in such cases, the financial firm must give the complainant at least 7 days' notice of the default to give them the chance to raise any defence they may have related to that default.

2.5 Making third party settlements

How are the complainant's rights affected in a third-party settlement?

An issue can occur where a complainant may have a claim against more than one party for their loss, but the complaint is only brought against one of those parties.

For example, a mortgage broker may have misled the complainant about a loan interest rate. If the broker was the financial firm's agent, the complainant has a potential claim against both the financial firm, for the conduct of the broker, and the broker.

The overarching principle is that you cannot be compensated twice for the same loss. If a complainant settles their claim against one financial firm for the full amount of their loss they generally cannot claim again from another.

However, if the complainant has not been fully compensated, they may wish to claim the remainder of their loss from another party.

Terms of settlement will often be in broad terms, such as the complainant agreeing not to bring any claim in any forum for that complaint. Depending on the wording of

the original settlement, it could prevent the complainant from pursuing a complaint about the same issues against other parties.

Unless the terms of settlement are very clear, we will interpret terms of settlement as only settling the complainant's claims against the other party to that agreement, and not against third parties. The complainant can make a further claim against third parties but cannot be compensated for more than the remaining loss.

Superannuation and family law settlements

AFCA does not resolve disputes about the allocation of superannuation interests between parties to a marriage for family law purposes. AFCA's superannuation jurisdiction is limited to reviewing the decisions (and related conduct) of superannuation providers in:

- implementing agreements or court orders that deal with a party's superannuation
- dealing with requests for information from a person who wishes to make an agreement or seek a court order dealing with a party's superannuation.

Under AFCA's superannuation jurisdiction, a person's spouse or former spouse can complain to AFCA that a decision or related conduct of the superannuation provider about the agreement, order or information request, was unfair or unreasonable if, for family law purposes, they are:

- party to an agreement
- subject to an order relating to that person's superannuation interest, or
- eligible to request information about that person's superannuation interest.

2.6 When will AFCA consider a complaint notwithstanding previous terms of settlement?

How can a previous settlement affect a new complaint?

Generally, where previous terms of settlement have been entered into between the parties to a complaint regarding the same subject matter as a subsequent new complaint, AFCA will not consider that subsequent new complaint.

However, in some circumstances, AFCA will review the previous settlement to determine:

- how it should be interpreted and whether it covers the same subject matter as a new complaint lodged with us, or
- whether AFCA should consider a complaint despite it being the subject of a previous settlement agreement.

Which principles of interpretation apply?

Principles for interpreting terms of settlement are summarised by J Santow in *Karam v ANZ Banking Group* [2001] NSWSC 709 at [406]. They are that:

- 1 The terms of settlement are to be interpreted as conveying the meaning that a reasonable person with the same background knowledge as both parties reasonably had when they signed it.
- 2 General words in the terms of settlement are limited to what the parties specifically considered the words to mean when they reached their agreement.
- 3 Generally, the parties did not intend to surrender rights and claims they were not aware of having when agreeing to the settlement.

This is why we interpret general words in terms of settlement that release the financial firm from all liability as a release only from liability for issues relating to the settled complaint. A general release does not apply to a further claim on a different matter.

When AFCA will consider a complaint despite it being the subject of a previous settlement agreement

Where terms of settlement have been previously agreed between parties, AFCA may consider a complaint that the settlement was obtained by fraud, duress, or misleading and deceptive or unconscionable conduct and is therefore legally invalid. This would proceed on the basis that the terms of settlement itself did not and could not deal with a complaint about the conduct of the financial firm in obtaining that settlement.

Terms of Settlement that resolved previous AFCA complaints

AFCA will not consider again a complaint that it has already dealt with (including under a terms of settlement) unless:

- there are additional events and facts that the complainant did not know, and could not reasonably have been expected to know, at the time the previous complaint was settled
- the additional events and facts are so significant that it would not be fair in all the circumstances to allow the settlement to stand.

AFCA will also take into account whether there has been unreasonable delay in bringing the new complaint.

Examples of additional events and facts that would justify AFCA considering the complaint again include the following:

- if AFCA is satisfied that the settlement agreement had been obtained by and is legally invalid due to fraud, duress, misleading, deceptive or unconscionable conduct or other compelling reasons

- if the settlement is manifestly disproportionate to the financial firm's and/or AFCA's approach to other similar type complaints and complainants
- if the scope of the terms of settlement or the conditions it imposes on the complainant go beyond what AFCA considers acceptable (see section 2.1 of this Approach) or are inconsistent with the AFCA Rules – for example, if the release of liability goes beyond the issues being considered in the AFCA complaint.

Terms of Settlement that resolved predecessor scheme complaints

Subject to limited exceptions, AFCA cannot consider a complaint that has already been dealt with by a court, dispute resolution tribunal established by legislation or a "Predecessor Scheme" (the Financial Ombudsman Service (FOS), the Credit and Investments Ombudsman (CIO), and their predecessors) – even if new information has since come to light.

Where terms of settlement have been approved by a court or statutory tribunal and resolved legal proceedings in that forum, AFCA cannot and will not go behind the court's order and will not consider the issues covered by that settlement. Parties that wish to challenge terms of settlement they made to resolve legal proceedings will need to do this in the appropriate court or tribunal.

Where terms of settlement resolved a Predecessor Scheme complaint, AFCA may consider a complaint that the settlement was obtained by fraud, duress, or misleading and deceptive or unconscionable conduct.

This would proceed on the basis that the terms of settlement itself did not and could not deal with a complaint about the conduct of the financial firm in obtaining that settlement.

If the complaint about the conduct resulting in the settlement agreement results in

- an agreement to allow AFCA to consider the underlying complaint, or
- a decision by AFCA that the agreement was so tainted by the firm's conduct that it was legally invalid, and therefore a conclusion that the complaint hadn't been "dealt with"

then AFCA would be able to consider the underlying complaint (subject to its jurisdiction under the Rules more generally).

3 Context

The case studies below are based on determinations by AFCA and its predecessor schemes. 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.

3.1 Case studies

Case 1: Broad settlement terms allowed a further claim

The complainant had a home loan with the financial firm and fell into default after losing his job. After unsuccessfully negotiating with the financial firm to vary the loan repayments due to financial difficulty, the complainant lodged a claim with us.

The complaint was settled with an agreement the complainant could make lower monthly repayments for three years. The terms of settlement were broadly in satisfaction of 'all claims' against the financial firm.

One year later, the complainant lodged a further claim against the financial firm about being misled over the home loan interest rate. The financial firm argued we could not consider the complaint as the complainant had previously settled 'all claims' against it.

We took the view that despite this broad expression in the previous terms of settlement, it applied only to complainant's initial complaint with the financial firm over the lowering of the loan repayments.

We accepted that the complainant could make the further claim against the financial firm.

Case 2: Unfair settlement terms

The complainant opened a Contracts for Difference (CFD) trading account with the financial firm's former authorised representative. At the time they opened his trading account, they had no trading experience and did not understand the risks associated with CFD trading. Although they had suffered significant losses, they say the financial firm encouraged them to continue trading.

After they complained to AFCA's predecessor scheme FOS, they received a settlement offer from the financial firm representing approximately 40% of the confirmed losses. Representatives of the financial firm advised them if they did not accept the offer, the company would soon be liquidated, and they would receive nothing. They signed and returned the terms of settlement.

We reviewed the terms of settlement and found they contained unconscionable terms including:

- clauses requiring payment of liquidated damages (up to \$250,000) in some instances and in other instances repayment of the settlement amount for any breach of the settlement agreement whatsoever by the complainant
- recitals stating that upon receipt of the settlement sum, the complainant agreed to withdraw the complaint and would otherwise be in breach of the terms of settlement
- confidentiality and non-disparagement obligations that were unreasonably wide and did not allow for appropriate exclusions such as the complainant's legal, accounting and tax advisors and as required by law.

We also found the financial firm:

- was exercising undue influence and pressure when negotiating directly with complainants including using unfair tactics to compel complaints to settle their claims and accept the amount and terms offered
- offered amounts which were unfair considering how AFCA would approach the issue of loss as outlined previous determinations AFCA had issued against the financial firm at that time in relation to substantially similar claims.

AFCA required the financial firm to ensure all further settlement offers were made in accordance with AFCA's approach to settlement and highlighting the inconsistencies outlined above. We also reported our concerns about the firm's terms of settlement and negotiating tactics to ASIC for investigation in accordance with AFCA's statutory obligations.

3.2 References

Definitions

Term	Definition
AFCA	the Australian Financial Complaints Authority
complainant	individual or small business that has lodged a complaint with AFCA
financial firm	a bank or credit provider who is a Member of AFCA
Rules	The AFCA rules which along with the Corporations Act govern AFCA's jurisdiction, powers and procedures

Useful links

Document type	Title / Link
Rules	afca.org.au/rules

Document type	Title / Link
Case law	McDermott v Black (1940) 63 CLR 161.
Case law	Osborn and Bernotti v McDermott [1998] 3 VR 1.
Case law	Masters v Cameron (1954) 91 CLR 353.
Case law	Zenith Engineering Pty Ltd v Queensland Crane & Machinery Pty Ltd [2000] QCA 221.
Case law	Duffy Bros. Fruit Market (Campbelltown) Pty Ltd v Gumland Property Holdings Pty Ltd [2007] NSWCA 7.
Case law	Karam v ANZ Banking Group [2001] NSWSC 709 at [406].