The AFCA Approach to financial difficulty: working together to find solutions

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

This document sets out our approach to Financial Difficulty complaints. The approach has been adopted from AFCA's predecessor scheme, the Financial Ombudsman Service.

When a consumer (an individual or small business owner) experiences financial difficulty, they will often ask their financial firm to help them with a repayment arrangement. Many successful arrangements are entered into regularly, but sometimes the consumer and financial firm are not able to agree on an arrangement that suits them both. That's where AFCA can help.

1.2 Summary

Who should read this document?

- Financial firms that deal with credit products, consumer representatives and consumers (individuals and small business owners), who are experiencing financial difficulty.
- Anyone who wants to understand how to work together to resolve financial difficulty, including working with AFCA if a complaint is lodged with us.
- Consumers and their representatives who may have a proposal which will see their financial difficulty overcome, as well as consumers who may be unable to identify a way forward.
- Anyone faced with dealing with financial difficulty that may not be able to be overcome in the short or medium term.

Summary of AFCA Approach

Financial difficulty occurs when a consumer is unexpectedly unable to meet their repayment obligations. This can be due to a number of causes including accident, separation, death of a family member, unexpected medical or funeral expenses, reduction of work hours, redundancy, or a downturn in business.

A large number of financial difficulty complaints that come to us are resolved by mutual agreement. The best solutions are often found when the parties work together to develop a plan for overcoming financial difficulty. For this reason, we encourage the parties to be willing to communicate and exchange information with each other.

Any requests made by the financial firm for information should not be so complex or large that it is overwhelming for the consumer. This is because excessive requests for information are often a barrier to providing hardship assistance and may prevent the early resolution of financial difficulty complaints.

A consumer should respond promptly to a financial firm's reasonable requests for information, and make payments if possible. For example, if a consumer has suggested a repayment arrangement that has been rejected by the financial firm, they should at the very least make repayments of the offered amount while we are considering the complaint.

The same principles apply when a financial firm assesses a request for assistance from a small business as when the request comes from an individual consumer. However, the information that a financial firm will need to genuinely consider a small business financial difficulty request will be different and may be more extensive.

In some complaints it is clear that financial difficulty cannot be overcome with further assistance, even in the longer term, and the only realistic solution is the sale of an asset such as a home or investment property. In these circumstances we will encourage the parties to agree on a reasonable timeframe for the consumer to sell the asset voluntarily.

In order to reach a successful and lasting outcome, it is important that all parties understand what is required of them. If a hardship arrangement is agreed to, it is good industry practice for the financial firm to confirm it in writing.

Depending on the circumstances, including the type and length of remaining term of the credit contract, a short-term solution may not be appropriate. The aim of any repayment arrangement should be for the debt to be repaid, even if that happens over a longer period.

A credit provider is under no obligation to waive debt on the grounds of financial difficulty alone. If the parties agree to temporarily suspend repayments the financial firm does not have to agree to waive interest or debt.

2 In detail

2.1 The AFCA Approach

A financial firm should assess each request for assistance on an individual basis. Solutions offered to the consumer need to be appropriate to the individual circumstances of that particular consumer. We encourage all parties to look at the broader situation when thinking of the available options for assistance. It may be that a consumer is focused on one facility when in fact they hold multiple facilities with the financial firm. By considering all facilities, a more robust solution may be found.

A consumer should be willing to start making repayments at the amount they've proposed under a repayment arrangement, even if the financial firm has not yet agreed to the arrangement. This demonstrates good faith and a willingness to deal with the financial difficulty.

2.2 Working together – reaching a resolution

The best solutions are often found when the parties work together to develop a plan for overcoming financial difficulty. For this reason, we encourage the parties to be willing to communicate and exchange information with each other.

Depending on the circumstances, a financial firm may need to ask the consumer for information about their financial position. This may include details of their income, expenditure and debts held with the financial firm and other financial institutions. We consider that reasonable requests for information are an important step to helping a consumer overcome their financial difficulty.

A financial firm should work to identify the available options, even when a consumer is yet to provide the requested information.

But, any requests made by the financial firm should not be so complex or large that it is overwhelming for the consumer. This is because excessive requests for information are often a barrier to providing hardship assistance and may prevent the early resolution of financial difficulty complaints.

To make an initial assessment, it is generally not necessary for a financial firm to request copies of rental agreements, medical certificates, bills or rates notices. The exception would be if there is a particular reason for the financial firm to doubt the information provided by the consumer.

Unless there is a valid reason why the documentation is not available, a consumer should be willing to support their request with relevant documentation.

If a consumer does not provide information, the financial firm should still work to identify what options are available with the information it does have, even if this information is limited. If the consumer's primary banking relationship is with that financial firm, the financial firm will have a lot of information available to it already which can be used to make an assessment.

If a financial firm doesn't have all the necessary information and needs to make some assumptions, it should state what assumptions it has made. For example, the financial firm could assume that the monthly wages figure the consumer has given is accurate, even though the consumer may not have provided payslips.

If the financial firm is unable to agree to a repayment arrangement based on the information available, it should provide the consumer with written reasons for its decision. The financial firm should also identify what, if any, additional documentation it requires from the consumer in order to reconsider its decision.

Providing detailed written reasons lets the consumer assess whether they can meet the financial firm's requirements and decide whether to make another proposal to resolve the situation. In other words, providing reasons to the consumer allows the conversation to continue so that the parties can work together to try and reach a solution.

2.3 Working together – small business

A small business's financial difficulty may be caused by a variety of events, including bad debts, loss of clients, increased competition or unexpected changes in market conditions. Common issues that we see in small business complaints about financial difficulty include the financial firm's entitlement to cancel business facilities, appoint an investigative accountant, apply an increased risk margin or charge higher interest rates.

Relevant industry codes, internal hardship policies and good industry practice require financial firms to work with their small business customers in the same way as for individual consumers, even though the causes of the financial difficulty may be different. This means that a financial firm should genuinely consider any request for assistance from a small business customer, following the principles set out in section 2.2 above.

When assessing a request for assistance from a small business, the nature of the information that the financial firm will need to ask its customer to provide will be different from and often more extensive than for individual consumers. This would include information that will allow the financial firm to consider the viability of the business as a going concern, for example:

- a revised business plan
- cash flow statements and projections, profit and loss and balance sheet information
- inventory management records, including opening/closing inventory levels
- gross profit projections
- aged debtor and creditor listings
- documentation relevant to the small business's statutory obligations including payroll, taxation, superannuation, GST and WorkCover records.

Similarly to individual consumers, if a small business does not provide all the information requested then the financial firm should still work to identify what options are available based on the information it does have, and state what assumptions it has made.

There will often be many options available to a financial firm to assist a small business, for example a temporary increase in an overdraft facility limit, deferment of scheduled repayments, the appointment of an Investigative Accountant, and consolidation or restructure of facilities. Where further lending is being considered, the financial firm will need to be mindful of its responsible lending obligations. The aim of any assistance should be to allow the small business to operate as a going concern in the long term.

While it is a commercial decision for the financial firm whether it applies an increased risk margin or default interest rate, it is generally not appropriate to do so when the business is already experiencing financial difficulty and is working with the financial firm to overcome those difficulties.

It may also be appropriate for the financial firm to refer the small business to relevant government agencies, dispute resolution services and small business councils, including:

- AusIndustry is an Australian Government resource to support businesses
- Council of Small Business Organisations Australia (COSBOA) provides advice, grant information and venture capital assistance
- Australian Small Business and Family Enterprise Ombudsman (ASBFEO) is an alternative dispute resolution service for small businesses that are in dispute with other businesses and Commonwealth Government agencies.

2.4 Working with AFCA

If the consumer and financial firm have not been able to resolve the complaint themselves, the consumer may choose to bring the complaint to AFCA.

We will consider a financial difficulty complaint by giving thought to how the financial firm has responded to the consumer's financial difficulty in the past. We will also look at the options available to assist the consumer to overcome their financial difficulty in the future. To do this, we require both parties to provide information to help us assess and investigate the complaint. The sooner we receive this information, the easier it is for us to help the parties negotiate a resolution.

AFCA will look at how well the financial firm responded to a consumer's previous financial difficulty and how the current situation can be overcome.

The information we often ask parties to send to us includes:

What we look at	What we need from the financial firm	What we need from the consumer
How well did the financial firm respond to the consumer's financial difficulty in the past?	• Contact records showing details of discussions with the consumer about their requests for assistance. • Copies of correspondence showing how the financial firm responded to the requests for assistance. • Copies of any information the financial firm relied on to make its decision about providing assistance.	• A copy of any letters to the financial firm that show what assistance was requested, and when. • Details of why the consumer believes the financial firm has not met its obligations. • Details of any loss suffered as a result of the financial firm's actions, including supporting documentation if available.

What we look at	What we need from the financial firm	What we need from the consumer
	• A copy of account statements showing the history of payments, the balances outstanding and any default fees, charges or other costs debited to the consumer's account following the request for assistance. • If relevant, a copy of documents relating to legal proceedings, so that we can see the status of these proceedings and review whether or not we are able to consider the complaint.	
How can the current financial difficulty be overcome?	• Enough details of the loan/s to be able to perform calculations such as a loan amortisation schedule. • Details of any payment arrangement that the financial firm is prepared to accept. • Details of any additional information or other conditions that the financial firm requires before it will agree to a proposed repayment arrangement. • If the financial firm is not prepared to accept a payment arrangement, reasons for this decision.	• For an individual, a completed Statement of Financial Position showing full and accurate details of their current circumstances. • For a small business, information relevant to the request being made of the financial firm. • Details of how they expect their circumstances to change. • A realistic repayment proposal that will see the debt, including any arrears, repaid within a reasonable timeframe. • If they cannot afford a repayment arrangement, details of their alternative proposal (for example, a timeframe for sale of an asset).

We ask consumers in financial difficulty to provide us with a Statement of Financial Position (SOFP). We will often still progress a complaint even if we have not received an SOFP, including holding a telephone conciliation conference. This is because the consumer's situation can be discussed at the conference.

However, if the consumer does not provide an SOFP then it may limit the assistance options the financial firm will consider. Also, we will generally not require the financial firm to vary a credit contract if a consumer has not provided an SOFP. More information on our power to vary credit contracts can be found in our power to vary credit contracts approach document.

If a consumer has lodged complaints with several financial firms, we encourage sharing all information with all financial firms. This can help to resolve the complaints, because each file may contain information that is relevant to our assessment of each complaint. For this reason, we may require the consumer to sign a Multiple Financial Firm Authority form, which will allow us to share all the information with each of the financial firms.

2.5 It is in the consumer's best interest to pay what they can

A consumer should respond promptly to a financial firm's reasonable requests for information, and make payments if possible. For example, if a consumer has suggested a repayment arrangement that has been rejected by the financial firm, they should at the very least make repayments of the offered amount while we are considering the complaint.

Regular repayments can show that the consumer is able to service the debt, even if it is at a lower amount than the contracted payments. Not only will regular repayments reduce the amount of interest accruing, it may also result in the financial firm viewing the consumer's proposal more favourably.

It is also important for the consumer to continue making whatever payments they can. This is because interest and fees will continue to be charged while the financial firm is assessing their repayment proposal, and while AFCA is considering any complaint. This may mean that equity in a property will erode and the arrears will continue to increase. For this reason, if the consumer does not make payments then their position is likely to worsen, and may reach a point where the financial difficulties cannot be overcome.

2.6 When the financial difficulty cannot be overcome

In some complaints it is clear that financial difficulty cannot be overcome with further assistance, even in the longer term, and the only realistic solution is the sale of an asset such as a home or investment property. In these circumstances we will encourage the parties to agree on a reasonable timeframe for the consumer to sell the asset voluntarily.

In the case of a small business, if the business is unable to demonstrate ongoing viability then we would not expect a financial firm to accept further risk. In this case, the financial firm should consider allowing the business a reasonable time to refinance, or work with the business to sell assets and achieve an orderly winding up of the business.

The situation is likely to be more challenging for both financial firms and consumers if there is long-term financial difficulty and there are no assets that can be sold. We would not require a financial firm to waive debt on the basis of long-term financial difficulty alone, so in these circumstances the options available to a consumer may be limited.

2.7 Resolution agreements

In order to reach a successful and lasting outcome, it is important that all parties understand what is required of them.

A large number of financial difficulty complaints that come to us are resolved by mutual agreement. An agreement can be reached at any stage of our process before we make a written decision about the complaint. If a hardship arrangement is agreed to, it is good industry practice for the financial firm to confirm it in writing.

The arrangement should include as much detail as possible about what the parties have agreed to, the timeframe for the arrangement and when normal repayments will resume.

A settlement occurs most often in a telephone conciliation conference where an in-principle agreement is reached. Following the conciliation conference, we will confirm in writing what was agreed. The financial firm may additionally choose to prepare its own settlement agreement reflecting what was agreed.

In the AFCA Approach to terms of settlement[1] we outline several principles that financial firms should bear in mind when drafting settlement agreements. We consider the acceptance by both parties of a settlement agreement document ensures certainty for the financial firm and consumer about what has been agreed to and ends the existing complaint.

However, if an entirely new and unforeseen event of financial difficulty arises after the settlement has been agreed, the financial firm should review the matter with fresh eyes. You can read more about what happens when a consumer requires further assistance in our Approach to dealing with common financial difficulty issues[2].

2.8 Longer term financial difficulty

Financial difficulties may be short-term or longer term. The financial firm's obligations under applicable legal principles and industry codes are not limited to short-term difficulties. Depending on the circumstances, including the type and length of term of the credit contract, a short-term solution may not be appropriate and a longer term solution will need to be considered.

The aim of any repayment arrangement should be for the debt to be repaid, even if that happens over a longer period. This means that any repayment proposal should be reasonable and realistic and should not simply be postponing inevitable default.

We encourage participants not to be constrained by timeframes, but instead be open to exploring viable options that will see the financial difficulty situation overcome, even if this is over a longer period of time.

[1] AFCA Approach to terms of settlement (www.AFCA.org.au/approach)
[2] AFCA Approach to dealing with common financial difficulty issues (www.AFCA.org.au/approach)

Examples of longer term solutions include:

- Capitalisation of arrears, where the consumer is able to meet ongoing repayments but is not able to clear the arrears.
- Extension of the loan term, resulting in a permanent reduction of the repayment amounts.

While we encourage the parties to explore both short-term and long-term solutions, a credit provider is under no obligation to waive debt on the grounds of financial difficulty alone. If the parties agree to temporarily suspend repayments but the financial firm does not agree to waive interest or debt, the suspension should not be for so long that the debt becomes unmanageable in the long-term. Similarly, reduced repayments that are insufficient to repay interest should only be in place for a limited period, unless the financial firm has agreed to reduce or waive interest.

We are increasingly seeing complaints involving consumers in long-term financial difficulty. We acknowledge that these situations are particularly challenging for both consumers and financial firms. For this reason we are committed to continuing to develop our approach in this area through ongoing consultation with financial firms and consumer representatives.

3 Context

3.1 Case studies

The case studies below are based on determinations by one of AFCA's predecessor schemes, the Financial Ombudsman Service (FOS), in which awards were made for non-financial loss. 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.

Case 1: When financial difficulty cannot be overcome

Max and Susan, who were farmers, brought a complaint to FOS. Their farm had been affected by drought and the loan secured over the farm property had fallen into arrears of $100,000. Over a number of years, the financial firm tried to assist them with various repayment arrangements, however, they were unable to return to making full repayments.

We conducted a telephone conciliation conference and the couple acknowledged that the only option was for the farm property to be sold. The parties agreed that Max and Susan would have an extended period of time to sell the property because this allowed them to complete the next harvest and use this income to reduce their debt as well as ensuring the farm remained operational through the marketing campaign.

Case 2: A consumer should pay what they can while their proposal is being considered

Nick requested assistance when he was unable to make full repayments on his car loan, which had three years remaining. He provided the financial firm with a Statement of Financial Position (SOFP) that showed that he could afford repayments of $120 per month if the loan term was extended by a further year.

The financial firm declined to vary the loan term and sought additional information from the consumer, including a statement from his non-English speaking partner regarding the payment of household expenses.

Nick lodged a complaint with FOS. FOS contacted the financial firm and noted that the proposal put forward appeared to be reasonable based on the information held by the financial firm. This was because the SOFP showed that:

- Nick could afford repayments of $120 per month
- he had been making repayments of this amount for several months, and
- the extension of the loan term by one year would see the remaining debt repaid.

FOS considered that Nick had demonstrated an ability to repay the debt if the contract was varied. Therefore, it was appropriate for the ombudsman to exercise his power to vary the credit contract if a resolution was not reached between the parties.

The financial firm reconsidered its position and accepted Nick's proposal without the need for further information. The resolution was formalised in a settlement agreement.

Case 3: Small business financial difficulty

John and Michael owned a retail store which had previously experienced a period of growth, financed by the small business through debt. Over time the small business became concerned that it would be unable to service its trade facility, and elected to sell assets which acted as security for the facility.

The repayment in full of the trade facility following the sale of the assets put the long-term viability of the business in jeopardy, as it was at risk of being unable to meet its short-term obligations. In accordance with the lending agreement, the financial firm appointed an Investigative Accountant for the purpose of gaining a better understanding of the business and what options were available. John and Michael were concerned about the cost of this review.

FOS conducted a telephone conciliation conference between the parties to explore the options. At the conciliation conference, the parties agreed to a progressive reduction of facilities over time, to enable the business to continue trading. In addition, arrangements were put in place to enable a third party to inject further funds into the business. The conclusions in the Investigative Accountant's report formed the basis of the agreement reached. By obtaining the report, the parties were able to gain a clearer view of the long-term direction and viability of the business. The financial firm also agreed to refund half the costs of the Investigative Accountant as a gesture of goodwill.

3.2 References

Definitions

Term	Definition
CBP	Code of Banking Practice
Complainant	A consumer who lodges a complaint at AFCA against their financial firm
Complaint	A complaint lodged at AFCA by a Complainant about the actions of their financial firm
Consumer	An individual or small business owner who uses the services of a financial firm
Credit contract	A credit facility provided to an individual or small business which may include a consumer credit contract
Financial difficulty	A consumer (individual or small business owner) may experience financial difficulty if they are unexpectedly unable to meet the repayment obligations on a credit contract
Financial firm	A bank or credit provider who is a Member of AFCA
SOFP	Statement of financial position is used to provide current and accurate details of all aspects of a consumer's financial position

Useful links

This document is one of a series we have produced about financial difficulty. We have also created documents which cover:

- how AFCA approaches financial difficulty, taking into consideration legal principles, industry codes and good industry practice
- dealing with common issues
- our power to vary credit contracts
- early release of superannuation.

All five documents can be found on our website[3].

[3] www.afca.org.au/approach

The following sites provide useful information to help people experiencing financial difficulty:

Document	Title / Link
MoneySmart	Australian Securities and Investments Commission's MoneySmart website www.moneysmart.gov.au
Doing it tough	Australian Bankers' Association 'Doing it tough' website www.doingittough.info
Financial Counselling Australia	www.financialcounsellingaustralia.org.au
Code of Banking Practice	http://bit.ly/291ZkqN/

The following sites provide useful information for small businesses:

Site	Link
AusIndustry	www.business.gov.au
Council of Small Business Organisations Australia	www.cosboa.org.au
Australian Small Business and Family Enterprise Ombudsman	www.asbfeo.gov.au