



The paper trail - worth its weight in gold!

I expect there are few advisers today who do not recognise the importance of having a good paper trail to confirm their dealings with clients, product providers, licensees, etc.

However, it is evident from the contact that I have with advisers and reviewing their files, that recognising the importance AND actually doing something about it are often two very different things.

This article looks at 2 aspects of this:

1. Is a good paper trail really that important?
2. Some practical tips to improve your record keeping.

Is the paper trail that important?

A story first. Some years ago, I was conducting a review of a financial planner who provided advice in a range of areas but had particular expertise in life insurance. I'll call him John Sure. John was a large writer for several companies but his compliance regime, and paper trail in particular, was poor.

Like many advisers, John appeared to understand the need for better record keeping but it was not the way that he had operated in the past and besides, he said, *"I have never had a complaint from a client"*. In our initial discussion, John complained of the extra burden of regulation (this "regulation" was the Life Insurance Industry Code of Practice; not FSR!!) and said that recording in writing all his dealings with clients would lead to an enormous time cost - time he did not have.

After reviewing some files which confirmed the worst, we had a further discussion. Prior to this discussion, John politely asked me if I would mind if he took a call from a

client that he was expecting in the next half hour or so. A short time later, as expected, the client called and John took the call. John leant back in his chair, put his feet on the desk and proceeded for the next 5-10 minutes to carefully listen to the client and provide him with what appeared to me to be sound and appropriate advice. He clearly had a thorough understanding of his client's circumstances, the strategies required and the products which would suit his client's needs.

The call concluded and we continued our discussion. After a little while, I asked John what he was going to do in relation to documenting the contents of the phone call that he had taken in my presence. His response was not unexpected. *"That's exactly what I mean. I now have to spend 5 minutes writing out a summary of my discussion with the client. I just don't have the time - although I know I have to make time."*

We'll come back to John shortly.

A clear paper trail of your dealings is a great way to manage particular risks that might occur in the absence of clear record keeping. When I refer to the management of risks, I am not just thinking of bad things that can happen. I am also referring to the potential loss of an opportunity. Let me explain.

The Australian and New Zealand Standard on Risk Management¹ defines "risk" as the *'the chance of something happening that will have an impact on objectives'*. Many of you who are AFSL holders will be familiar with this Standard and the concept of risk as you will have carried out a risk management assessment as part of your application for the AFSL.

Even if you are not an AFSL holder, prudent financial planning businesses will have documented business plans which they review at regular intervals. (Terry Bell of *Business Health* advises that of 750 financial advising businesses who have

¹ AS/NZS 4360:2004

undergone the *Business Health* Health Check diagnostic, 53% do not have a clearly documented and current business plan for their business. Furthermore, the annual profit/principal of those that do is \$140,326 compared to \$72,534 of those that don't!)

These business plans would hopefully set out objectives which address the current and future operations of the business. So, I would expect that objectives would include amongst other things:

- goals in relation to the quality of the services provided to clients;
- the strategic focus of the business;
- marketing objectives;
- financial objectives.

In relation to the financial objectives, most financial advising firms will consider sale of the business an option "down the track" in which case, clearly the best possible price will be sought. Put yourself in the shoes of a prospective purchaser of a financial planning practice. What will they rate highly? Obviously the amount of in-force business will be critical as will the other resources of the business such as staff, equipment and goodwill. However, purchasers are also looking for a quality book as opposed to a list of clients. Ideally, this will include client files which will tell a complete and accurate story about each of the vendor planner's clients.

A review of a sample of files should enable the prospective purchaser to satisfy themselves that each file will be able to answer the following simple questions:

1. What is the history of the firm's dealing with the client?
2. What is the current position?
3. What needs to be attended to going forward and when?

These questions will only be satisfactorily answered if the paper trail is complete. The failure to do so might jeopardise a potential sale and thereby runs the risk of failing to maximise the opportunity to sell the business/book for the best possible price.

Back to John.

As I mentioned, he was a large writer and had an extensive book. But what would he be selling? He may, of course, have had a Buyer of Last Resort agreement upon which he may have been relying (although such agreements should make the BOLR subject to satisfactory compliance and record keeping practices). But what if he didn't or there was a buyer willing to pay more than the BOLR, subject to a due diligence?

On the basis of the review of the small sample of files I saw, it would be impossible for a prospective purchaser to know precisely what they were buying. The business might have been OK but in the absence of clearly documented files, the purchaser might have been buying a pile of risks or "ticking time bombs". In my discussions with advisers, few are willing to take on such risks.

In summary then, by not changing his procedures and 'leaning back in the chair', John may have been missing out on an opportunity – the opportunity to sell his register for the best possible price. If, however, instead of leaning back, he had leant forward, put the phone in his left hand, pen in his right hand and bullet pointed his discussion with his client, the file note would have been recorded at the same time as the conversation and no extra time would have been taken. In doing so he would have better managed this risk.

He would also have better managed the risk of a dispute with the client and the threat of a claim or litigation.

Imagine that the telephone discussion with the client that I overheard followed a

meeting with the client (let’s call her Mary Poole) and her husband (Peter) a week or two earlier. In that meeting, the second meeting with the clients, John had taken them through the Statement of Advice he had prepared after the first meeting. The SoA recommendations reflected a reasonably aggressive risk profile which was at odds with Mary’s profile. However, John later discussed this with Mary in a telephone conversation. Mary agreed to go along with the recommendations because her husband, Peter, thought it would be OK.

Some time later, Peter died from cancer and after obtaining advice, Mary issued proceedings against John, John’s Corporate Authorised Representative business and the Licensee for failing to give appropriate advice. One limb of the claim was that the investment recommendations were inappropriate given Mary’s risk profile, the investments had ‘headed south’ and Mary had suffered further loss.

When giving evidence, Mary denied having a telephone conversation with John in which she authorised him to proceed on the basis of Peter’s risk profile.

In the witness box, John reiterated his claim that he had discussed this very issue with Mary and she had given him the go-ahead. The cross-examination might have run something like this:

Counsel for Mary	Let’s go back to the Statement of Advice you prepared for Mr & Mrs Poole - exhibit P2. Please turn to page 6, headed “Investment risk and capital volatility” and read the paragraph under the heading.
John	“Mary, based on the information you have provided, your Risk Profile is Conservative. This means you seek a solid income stream with growth opportunities being of a

	secondary consequence. The portfolio would be weighted towards income bearing securities such as cash and fixed interest, with a small exposure to equities and property providing appreciation potential.”
Counsel for Mary	What % of the portfolio did you recommend should be placed in Australian and international shares?
John	<i>[Whispers]</i> Approximately 93%.
Counsel for Mary	I’m sorry. I didn’t hear you.
John	<i>[louder]</i> 93%.
Counsel for Mary	So your recommendation did not suit Mrs Poole’s risk profile?
John	No, but it suited Mr Poole’s risk profile and there is no way they would get the returns they were after with conservative investments. Plus I got the go-ahead a day or 2 later to follow Peter’s risk profile in the telephone conversation I had with Mary. I was advising them as a couple.
Counsel for Mary	Ah yes. The telephone call. My client has denied in evidence that she had any such call from you after the meeting.
John	But I did, I remember it well. I spoke to both of them and they were happy for me to proceed on the basis of Peter’s profile.
Counsel for Mary	Do you have a record of this telephone conversation?
John	Err, no.
Counsel for Mary	So, Mr Sure, you are asking the court to believe that you had a telephone conversation

	<p>with my client and her late husband which my client denies ever took place. Furthermore, you have no written record of this conversation to support your assertion.</p> <p>No further questions, your Honour.</p>
--	--

Clearly, John’s position would have been stronger if he had a file note summarising his discussion with Mary and Peter and which he could confidently assure the court was made contemporaneously with the time of the call. The position could have been further improved if John had sent a letter or email to Mary and Peter confirming their discussion.

A few tips

- ‘Just do it!’ Your files should tell a story and that will only be the case if copies correspondence, emails, schedules, receipts of FSGs, acknowledgements, file notes of telephone calls and meetings are retained on the file.
- Produce a pad with your logo and prompts for details so that when you meet with the client, you can record your discussions in bullet point format. Prompts might be date, starting and finishing time of meeting/phone call (you can now tell this article was written by a lawyer!), who was present, location of meeting, telephone in, telephone out, telephone number, etc.
- Record the information so that you would be happy for your mother (or a court) to read it. Inflammatory or derogatory comments found in documents produced in the discovery process in litigation are rarely helpful!
- Email is a great way to communicate with clients and other parties. However, it is also a “conversational” means of communication which can come back to bite you. I recommend

that a degree of formality be retained in emails.

- With documents such as Statements of Advice, make sure that they reflect accurately your advice to the client. Most advisers use templates and in my experience of reading numerous SoAs, Customer Advice Records and Financial Plans, that’s often what they look like – templates with extensive cutting and pasting. The SoA which speaks directly to the client in normal language and clearly links the recommendations to the client’s circumstances is a rare gem.
- Electronic records are easier and cheaper to store, duplicate and search. They can also reveal information “behind” the material, (which is also called “metadata”) such as information about when the record was created, the author, and a history of the amendments to the document, for example the “track changes” function. This can present both advantages and risks.
- If you need to rely upon e-files in the context of litigation, it is important to ensure that the information is not accidentally altered or deleted (for example, ensuring that computer macros do not automatically change the date of a document when accessed).
- When deciding which electronic documents are relevant to a dispute, remember to consider deleted emails (which may be relevant), and different versions of emails (for example, the “received” version and the “sent” version).
- Signing and dating documents such as file notes, fact finders and even SoAs is a very sound practice (and may be required by your licensee) but if you forget to sign them or it is inconvenient to have the client sign them, don’t despair. In many years of legal of practice, I can’t recall ever asking a client to sign my advice to them or the

notes which I have taken as a basis for the advice - nor would I expect them to!

- The alarm bells should ring when you are dealing with a client and the situation is or the client makes a request which is “out of the ordinary”. To use a simple example, when giving advice in relation to an income protection policy, the adviser should explain why they have recommended a particular wait and benefit period. The need to do so is even greater when your recommendation includes a wait period of other than 30 days or a benefit period other than to age 65.
- Don’t throw out your “rough” notes such as calculations, memos and diagrams. These are often a critical factor in demonstrating the basis of the advice to the client and should not be discarded because they look a little untidy or because the information might be contained in the SoA. These are often the notes which are made contemporaneously with your dealings with the client and therefore have significant evidentiary value in court. (Mind you, if they are on the back of a drink coaster, it might be prudent to reproduce them elsewhere)!

“Is the paper trail important?” You bet but seeing it as your friend and not a burden is half the battle.

The law is current as at December 2007.

Please note that this paper is a summary of the law only and is not a substitute for legal advice. Holley Nethercote is able to assist companies in meeting their obligations in this area by providing practical and prompt legal advice. Licensing, training and creation of compliance programs are also available via an associated business, Compact- Compliance and Corporate Training – www.compliance-training.com.au.

We invite you to contact us:

Telephone: (03) 9670 8200

Facsimile: (03) 9670 5499

Email: law@holleynethercote.com.au

Web: www.holleynethercote.com.au