



ASIC RAMPS UP ENFORCEMENT OF 'BEST INTERESTS' OBLIGATIONS

On 5 February 2018, the Federal Court fined three Melbourne based companies and their common director more than \$7,800,000 for breaches of the financial services law.

BY GINA BOZINOVSKI, SPECIAL COUNSEL
and ANDREW DAVIES-EVANS, LAW GRADUATE

FEBRUARY 2018

The Federal Court held that Wealth and Risk Management Pty Ltd (**WRM**) and its related entities Jeca Holdings Pty Ltd (**Jeca**) and Yes FP Pty Ltd (**Yes FP**), together with their common director, Mr Joshua Fuoco (**Mr Fuoco**), engaged in significant breaches of the financial services law and made the following orders:

- \$7,150,000 worth of penalties against WRM, Jeca and YES FP; and
- \$650,000 against Mr Fuoco for knowingly being concerned with the breaches.

In addition, Mr Fuoco agreed to a declaration and orders restraining him from providing financial services for 10 years, and to pay \$100,000 towards ASIC's costs.

The case (or series of cases more appropriately) played out like a Hollywood production complete with the requisite sequel. It begins with the initial proceedings against a number of entities, follows up with a sequel proceeding against related entities and parties and ends with an almost \$8million order.

The Story Begins – the WRM Proceedings

In March 2017, ASIC commenced proceedings against WRM, Jeca, Yes FP (collectively the **Fuoco Group**) and Mr Fuoco for alleged breaches of the financial services law (**WRM Proceedings**).¹

Specifically, ASIC claimed that the Fuoco Group operated a scheme whereby:

- (a) The Fuoco Group offered clients fast cash loan, targeting consumers with poor credit histories through online web advertisements;
- (b) In order to obtain the funds, the Fuoco Group required clients obtain and pay for financial advice from a WRM authorised representative;
- (c) The financial advice was almost always to recommend that clients switch their superannuation and insurance;
- (d) In order to obtain the funds clients were required to comply with the advice;
- (e) A trailing commission was received by the Fuoco Group in addition to the charging of the advice fees;
- (f) The Fuoco Group paid the client part of the trailing commission it received.

In the court's judgement, it was found that WRM's representatives were paid bonuses upon the number of applicants solicited per month, incentivising WRM employees to convince applicants to transfer funds and policies entirely irrespective of their specific financial circumstance.

On transferring funds and purchasing the recommended policies, WRM would then receive a commission from these new insurance/superannuation entities, and from this commission the 'cash rebate' would be provided to the applicant. The new policies often charged steep premiums that were entirely unsuitable in light of the applicant's financial condition.

Independently, WRM would also charge a 'financial advice fee', which was withdrawn from the client's superannuation balance. This advice fee often outweighed the size of the original credit amount being requested by the client.

Between October 2015 and March 2016, 901 applicants received financial services and advice under this scheme. The court subsequently granted injunctions to restrict all defendants from making offers of cash payments, and from providing financial statements of advice, due to numerous contraventions of the best interests provisions.

On May 2017, ASIC was granted an injunction in the WRM Proceedings, pending the final hearing.

WRM, Jeca and YES FP ceased operating as a consequence.

Mr Fuoco and other individuals who had managed the Fuoco Group then decided to establish three new companies: CGF One Pty Ltd, EM J Two Pty Ltd; and Firemac Pty Ltd (together the **A3 Group**). The A3 Group ultimately failed as its business model relied upon the loans being provided by a third party and the third party did not approve the loan applications.

The Sequel – Financial Circle Proceedings

Now, bear with us because this is where things get even more interesting.

Following the failure of the A3 Group and the injunctions against the Fuoco Group, former employees of the Fuoco Group decided to set up an entity known as "Financial Circle Pty Ltd" (**Financial Circle**). Financial Circle's sole director and the entirety of Financial Circle's senior management staff consisted of former employees of the Fuoco Group. Financial Circle also initially operated out of the same premises as the Fuoco Group.

Financial Circle's scheme was by and large identical to that of the Fuoco Group, that is, a circle of loans, advice, insurance and superannuation changes targeting clients with poor credit.

Financial Circle was off to a strong start. In fact, between late August and mid-December 2017, Financial Circle advanced a total of 57 loans, with a total value of \$196,406. Each loan was accompanied by a Statement of Advice, for which Financial Circle charged an advice preparation fee of around \$5,000 (subject to variation). Clients were provided with advice which included insurance and superannuation recommendations.

Generally, the amount of the advice fee and/or the insurance premiums was greater than the amount of the client's loan.

Importantly, all of Financial Circle's senior management and its customer service offers had all previously worked for the Fuoco Group.

¹ *Australian Securities and Investments Commission v Wealth & Risk Management Pty Ltd* [2017] FCA 477

In addition, Financial Circle utilised a panel of private funders who provided the funding for the loans to clients. The Fuoco family was part of that panel. Of the 57 loans in place at least 30 had been funded by the Fuoco family.

In November 2017, Financial Circle came to the attention of the regulator and ASIC commenced investigations into suspected contraventions of the *Corporations Act* by Financial Circle and its directors and officers. ASIC brought an action against Financial Circle, describing it as "a sequel" to the WRM Proceedings (**Financial Circle Proceedings**).² The Federal Court again granted similar injunctions due to numerous contraventions of the best interest obligations.

On 10 January 2018, the Federal Court delivered its judgement in the Financial Circle Proceedings. Moshinsky J held that:

"[Financial Circle's] business model makes it practically impossible for authorised representatives to act in the best interests of clients, to provide tailored and appropriate advice, to warn clients where advice is based on incomplete or inaccurate information, and to give priority to the client's interests as required by ss 961B, 961G, 961H and 961J of the *Corporations Act*.³"

The Court also held that it was appropriate to grant injunctions to restrain Financial Circle from engaging in the relevant conduct until the hearing.

The Finale

Circling back around, on 5 February 2018 the Federal Court made its order in respect of the WRM Proceedings. As noted in our introduction, the court held that WRM, Jeca, Yes FP and Mr Fuoco were liable for almost \$8million in penalties for numerous contraventions of the *Corporations Act*⁴ as well as the *Australian Securities and Investments Commission Act*⁵.

The court found WRM to be in breach of the best interests obligations, as well as in breach for failing to ensure their authorised representative, Yes FP, acted in the best interest of the client.

Jeca was held to have provided financial product advice without holding an AFSL, or being authorised to do so by another licensee. Jeca was held to have employed a number of sales representatives during the business' operation,

and was not an authorised representative of WRM. The internet advertisements offering "fast cash", published by Jeca, were also deemed to have been representations that were misleading or deceptive in nature.

WRM, Jeca and Yes FP were all deemed to have engaged in unconscionable conduct, in the provision of financial services.

Mr Fuoco was held to be knowingly involved in Jeca's provision of financial advice absent a license, the misleading and deceptive advertisements as well as the three defendants unconscionable conduct.

WRM, Jeca and Yes FP were ordered to collectively pay \$7,150,000, with Mr Fuoco to personally pay \$650,000 for being knowingly involved in the contraventions, and to cover ASIC's cost in investigating the matter. Mr Fuoco has also been restrained from providing financial services for a period of 10 years.

The Order was made separately from the Financial Circle Proceedings, which we understand to still be before the courts.

Outcome

This series of cases demonstrates that ASIC is shifting into gear in enforcing the best interest obligations required of financial advisors. In light of ASIC's apparent willingness to prosecute 'best interests' contraventions, if you are a provider of financial advice, it is now essential to ensure that you have adequate and appropriate policies and procedures to demonstrate a compliance with 'best interests' duties required under the *Corporations Act*.

For more information about these cases, financial services law, or advice regarding ASIC, please contact Gina Bozinovski.

GINA BOZINOVSKI
Special Counsel, Corporate & Commercial
D (07) 3223 9102
E gina.bozinovski@brhlawyers.com.au

² *ASIC v Financial Circle Pty Ltd* [2018] FCA 2

³ *Ibid* at paragraph 92

⁴ *Corporations Act 2001* (Cth) ss 911A, 912A(1), 961G, 961J, 961L, 1041H

⁵ *Australian Securities and Investments Commission Act 2001* (Cth) ss 12CB, 12DA, 12DB