Beware the pitfalls lurking in a statement of advice

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When a financial planner provides you with advice, you must be given a document called a statement of advice or SOA. The idea behind a SOA is to give you important information about the advice so that you can make an informed decision about whether to act on it. In reality, SOAs are used by financial planning firms to limit their liability for poor financial advice.

Clients make complaints against their financial planners because they have suffered a loss as a result of acting on advice set out in the SOA. Clients suffer losses because an unexpected event occurs, for example, a company that they have invested in fails.

In the financial world, unexpected events happen every day and every day clients lose as a result of them. This means that every investment that you make has some risk associated with it. It is this risk actually happening that has caused you to suffer a loss. For this reason, SOAs are heavily focused on risk to protect financial planners from potential liability for that loss.

When a client makes a complaint about a loss, the first thing that the financial planner or their lawyers will do is get out the SOA and use it to argue that the client fully understood the risk that caused the loss and was willing to take that risk. In making this argument, the lawyers will say four things.

The first is that the risk was explained to you in the SOA. Most SOAs contain numerous generic statements about risk that will be used to make an argument that you understood the risks that you were taking and were willing to accept them. These statements don't actually tell you anything that is useful. You need to ask your financial planner to document in the SOA what the risks are, how likely it is they will happen and why it is a good idea for you to take those risks.

The second is that your financial objectives were such that you wanted to take on a lot of risk so as to achieve a higher return. Every SOA will set out what the financial planner says are your financial objectives. Lawyers use these objectives to argue that because you wanted to achieve some objective, for example, that you would like enough money to go on an overseas holiday, you decided to accept a lot of risk to achieve that objective. You need to look very closely at the financial objectives section of the SOA to make sure that your financial objectives are properly described. If they aren't, ask your financial planner to change them.

The third is that you understood how risk works and were willing to accept high levels of risk. The SOA has a section dealing with how much risk you are willing to accept and you will be described as a particular type of investor, such as aggressive or assertive. SOAs often overstate clients' risk tolerance so you will be described as being willing to accept a lot of risk when, in fact, you are a conservative investor. You need to think carefully about whether you are the person described in the SOA and or ask your financial planner to change it.

The fourth is that you were told about the risk in the product disclosure statement. At the time that you are told about many financial products you must also be given a document called a product disclosure statement or PDS. A PDS is a document prepared by the company that is selling the financial product that you are thinking about buying.

The PDS sets out detailed information about the financial product including the risks that are associated with it. The risk section of a PDS will cover every conceivable risk using technical concepts that most people do not understand. Lawyers use this risk section to argue that you were aware or should have been aware of the risk that caused your loss.

The SOA will say that that you must read the PDS. Very few clients read a PDS and, even if they did, they wouldn't understand it. You should ask your financial planner to explain the risks associated with the financial product you are thinking about and to explain how likely it is that those risks will happen.

David Huggins is a lawyer who specialises in resolving disputes about poor financial advice