Association of Financial Advisers

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Ms Ai-Lin Lee
Policy Guidance Officer
Financial advisers
Australian Securities and Investments Commission
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Dear Ms Lee,

AFA Submission – Consultation Paper 216 – Advice on Self-Managed Superannuation Funds – specific Disclosure Requirements and SMSF Costs

The Association Of Financial Advisers Limited ("**AFA**") has been serving the financial advising industry for over 65 years. Its aim is to provide members with a robust united voice, continually improve practices and focus firmly on the exciting, dynamic future of the financial advising industry. The AFA also holds the client to be at the centre of the advice relationship and thus support policies that are good for consumers and their wealth outcomes.

With over six and half decades of success behind us, the AFA's ongoing relevance is due to our philosophy of being an association of advisers run by advisers. This means advisers set the agenda, decide which issues to tackle and shape the organisation's strategic plan.

Thank you for the opportunity to provide feedback on Consultation Paper 216.

We recognise the issues behind this Consultation Paper and the recent report on SMSFs (Report 337). We also appreciate the central importance of SMSF clients fully understanding what they are taking on when they establish a new SMSF. Thus we are supportive of some increases to the level of disclosure and a more complete consideration of the client circumstances that warrant a SMSF and the cost considerations in such a recommendation.

We are conscious that the increased requirements are significant and that these requirements will only apply to financial advisers and not to accountants who are recommending SMSFs under the accountant's exemption until the repeal of this exemption in July 2016. We are aware that this will further impact the lack of a level playing field when it comes to advising on SMSFs. As part of the Regulatory Impact Analysis (RIA), we believe that it is appropriate to examine the proportion of advice on the establishment of SMSFs that is provided by financial advisers relative to accountants. If financial advisers only comprise a small fraction of total SMSF advice, then it may be wise to wait until both financial advisers and accountants are operating under the same regulatory regime.

In terms of the process consumers go through in the establishment on an SMSF, it appears that an increasing number of consumers are going through on-line service providers and will receive no advice in this process. This is a group of consumers where we have a higher level of concern with respect to confidence that the right protections exist. Other consumers will initially receive advice from an accountant, and then go to a financial adviser for advice on some aspects of the establishment of the fund. The financial adviser will not always have a high level of control or influence over the overall process of the establishment of the fund. The financial adviser will often only provide advice on the investment of the SMSF funds and not the establishment of the fund. The different roles that a financial adviser might play in the advice process needs to be taken into account when considering the obligations of the financial adviser in the provision of SMSF advice.

The primary regulator of SMSFs is the ATO. We appreciate that ASIC is the regulator of "gate-keepers", however we note that there is no reference to the extent that these changes have been proposed in consultation with the ATO or independent of the ATO.

We note that ASIC proposes to make these changes by Class Order. We question the necessity to do this by Class Order rather than regulatory guidance, particularly in the context that these obligations will only apply to a segment of the SMSF advice market (i.e. financial advisers). We consider that the proposals can be adequately achieved by regulatory guidance.

There is an ongoing battle, in terms of Statements of Advice (SoAs), to ensure that there is the right balance between being concise and fully disclosing literally all potentially relevant considerations. Increasing the scope and size of SoAs involves a trade-off, given the material risk that the larger they are, then more clients are less likely to read them.

The product replacement obligations under section 947D of the Corporations Act already places significant obligations on the financial adviser to provide information on the costs and consequences of replacing one product (i.e. an APRA approved fund) with another product (i.e. an SMSF). Thus information on the costs and risks of establishing an SMSF, when the client will be transferring existing assets into the fund, is already required. Much of what has been proposed in this consultation paper is already being provided by financial advisers who specialise in SMSFs.

Our detailed responses to the questions raised in this Consultation Paper are set out below:

Warning clients about a lack of statutory compensation for SMSFs

We are supportive of the provision of this warning, however we do not believe it will have a significant impact and further believe that it is necessary to avoid overstating the underlying risk of fraud and theft relative to other risks that SMSF clients face.

Question	Response
B1Q1	We do not oppose the provision of a warning, when establishing or switching to an SMSF, that they do not have access to compensation arrangements under the SIS Act in the event of fraud or theft.
B1Q2	We believe that there are two key considerations in this proposal: • The warning is required at the time the SMSF is established, yet the risk is actually incurred at a later point when the SMSF invests in an asset that may not be subject to this protection. • Clients are often not very focussed upon the risk of fraud and theft in an underlying investment at the time of establishing an SMSF. It is to a large extent peripheral to the key risks in commencing and conducting a SMSF that clients focus upon in the establishment phase. Thus we don't expect that this warning will deliver significant benefits to clients as this is

Question	Response
	a risk that they are less likely to perceive as important within the many other aspects of commencing a SMSF trustee role. The other warnings that should be provided are either already provided or are addressed under Question B2.
B1Q3	As stated above, we are hesitant about increasing the scale of the SoA, and therefore suggest that this warning should be provided as part of a reference document on the risks of SMSF. We would be supportive of the industry developing a standardised risks disclosure document that could be provided to all SMSF clients. Therefore we would support a prescribed format in a stand-alone document(s). A statement within the SOA that the stand alone document has been provided to the client(s) would be acceptable.
B1Q4	Clients are not required to sign a declaration that they understand other risks when it comes to investing, whether that be through an SMSF or in any other form. We do not support the requirement for them to sign a declaration, which we think would likely run the risk of becoming counter-productive. If this specific risk requires the clients to sign a declaration, then it is giving a message that this risk is of a far greater scale than is the underlying reality.
B1Q5	If it was necessary to include this warning in an SoA, and clients were required to sign a specific declaration of their understanding of this risk, then the costs to implement this change will be significantly greater. If the warning can be given as part of the provision of a standalone document(s) on the broader risks and considerations in the establishment of an SMSF, then the costs would be more manageable. Any change will require additional training and modification to processes, which will need to be provided to all financial advisers who provide SMSF advice.
B1Q6	We have addressed in the sections above all the practical problems that we envisage with this proposal.

Disclosure Requirements

With respect to these requirements, we are largely in agreement with what has been proposed however we believe that they should be achieved through the use of a stand-alone document(s) rather than the requirement to change SoA templates. We want to avoid the addition of a significant amount of non-personal information to the SoA. We continue to believe that SoAs should be as concise as possible and predominantly specific to the person rather than full of generic information.

Question	Response
B2Q1	We are broadly in agreement with what is proposed in Table 2, however we question why costs are addressed in terms of both item 5 in Table 2 and also Table 4 (Question C1). It seems that this obligation is duplicated. Whilst we are in agreement to these disclosures in general terms, there needs to be adequate consideration given to the most efficient means of providing these disclosures. We recommend that as much as is possible, this is done by reference rather than by increasing the size of an SoA. There is also a need to allow for the fact that some of these disclosures will be provided under separate obligations, whether this is the best

Question	Response
	interest duty or the product replacement obligations (s947D). We also do not support the proposal that these disclosures should be required through the means of a Class Order. We believe that release of the final disclosure requirements should be done via regulatory guidance as an appropriate use of ASIC's powers in this context
B2Q2	We believe that it will be beneficial for clients to be aware of this information prior to making a decision to establish or switch into an SMSF. It should be noted that some of these disclosures would already be provided to SMSF clients as part of existing advice processes and templates. For example many financial advisers who provide SMSF establishment advice will also be preparing an investment strategy for the fund.
B2Q3	We believe that this information should be given in a standalone document(s), rather than as part of the SoA. For this reason, we believe that the development of an industry endorsed document would be a valuable alternative. If this was the selected path then we would be supportive of a jointly agreed prescribed format. As an example, we refer to Item 1 in Table 2, which refers to the ATO disclosure document. All of this could be provided by the means of inclusion by reference. The ATO document could simply be a separate document provided with the SoA, rather than be incorporated into the SoA. Where the disclosure obligations are more personal in nature, such as specific insurance related considerations, then there is a better argument for inclusion in the SoA.
B2Q4	The ATO already requires new trustees to sign a declaration with respect to the responsibilities and obligations of an SMSF trustee. We do not believe that it is necessary to duplicate this requirement during the advice process, although we accept that the ATO process occurs at a later point. It is important that these responsibilities and SMSF specific risks are explained to the client, however we do not consider it necessary to extend this to the level of the client signing a declaration. It is not the signing of the declaration that is the objective, but the development of the knowledge and understanding. Signing a document does not prove that the trustee truly understands the obligations. As a general principle across the full spectrum of financial advice, we do not believe getting clients to sign declarations for a range of different issues is an appropriate strategy. Clients already sign a number of documents in the financial advice process. Further signatures are not likely to have any positive benefit in ensuring that the clients' knowledge and understanding of the issues has been achieved.
B2Q5	These additional disclosure requirements will contribute to increased costs at the licensee level in ongoing supervision of the requirement and the initial change to internal rules and procedures including SOA templates and adviser training, as well as at the adviser level in adapting the change and explaining additional elements within the SOA to the client. The level of the increase in costs will depend upon the extent to which these disclosures change SoA templates and the extent to which standardised industry disclosure documents can be developed. We are unable to calculate these costs or present them as figures. There will be costs at the licensee level and at the adviser level, thus the cost per adviser will vary depending upon the number of advisers in the licensee.

Question	Response
B2Q6	We have covered all the key practical considerations in implementing this proposal in the sections above.
B2Q7	Whilst we support the proposal with respect to the mention of an exit strategy from an SMSF, there will be a range of different reasons why an SMSF client will need to exit an SMSF in the future (divorce, mental capacity, insufficient funds). The exact reason for the future exit may not be apparent at the time the advice is provided. Thus rather than this being a specific strategy for the individual client, we suggest that this should be a standardised document on common scenarios for exiting an SMSF and the process and cost to achieve this.

Transitional Period

We are supportive of a sensible transitional period. We refer again to the point that we raised above that these obligations will only apply to financial advisers and not to accountants who are providing SMSF advice under the accountant's exemption. In this context, we think it is appropriate that the effective commencement date should be 1 July 2016. In any circumstance a minimum of 12 months should be provided.

Question	Response
B3Q1	The scale of the changes that are required depend upon the final outcome of this consultation process. Where there is a requirement to change SoA templates, even if it is just for the inclusion of a reference to a separate stand-alone document on the risks and considerations when establishing an SMSF, there is a need for a 12 month transition period. This is certainly the case at the present time where there are so many issues of greater significance impacting upon the financial advice industry. Larger licensees have release programs for SoA changes that are staggered, and there needs to be sufficient time available for planning, design, training and implementation. There are other changes that will be required that all take time to be designed and delivered. Where it comes to adviser training, this impacts advisers right across the country and thus it is appropriate to allow a longer time frame to ensure that this training can be delivered in an effective and efficient manner. We believe a minimum 12 month transition period is required although logically a commencement date of 1 July 2016 would facilitate consistency with the end of the Accountant's Exemption.

Guidance on costs

We recognise the importance of cost in the consideration of the establishment or switching to an SMSF. There is a need for some guidance to be provided to clients on this issue. We are supportive of the proposed guidance, based upon the Rice Warner research, and consider this a much better approach than the establishment of specific limits.

Question	Response
C1Q1	We appreciate that Rice Warner have considered the key costs in the establishment of an SMSF and have identified that different options exist in terms of the level of activity that is outsourced, and that this will impact the overall cost of the establishment and ongoing operation of an SMSF. We are aware that there are a range of service providers who will have different cost points, each of which will change over time. We believe that the ranges identified by Rice Warner are reasonable, although they may change over time as the cost of different services change. The SMSF services market has become increasingly competitive, and costs will inevitably change over time, which will impact upon this assessment.
C1Q2	This question is somewhat confusing as we believe that it should be left to the advice provider to provide guidance on costs rather than to have ASIC provide this guidance. We also believe that in giving guidance to a client it is more appropriate to provide a range of costs rather than a specific number. We note that a formal and regular process of updating this guidance would be required of ASIC to avoid misdirecting consumers on the issue. We do not believe that it is practical to provide guidance on the time cost associated with managing an SMSF. This depends upon the level of time devoted to the management of the fund (essential and voluntary) and the cost of that time, which will vary from person to person. Neither do we think that it is practical to cost the fact that an SMSF does not have access to compensation under the SIS Act. The differential in the cost of obtaining insurance under an SMSF, as opposed to an APRA fund will only be practical when the client is moving from an APRA fund to an SMSF, and also only when the client requests insurance quotes on the cost either within the SMSF or as a stand-alone ordinary life policy. If the client declines advice on insurance, then it does not make sense for the adviser to be required to obtain quotes solely in order to explain this to the client. We believe that this should be addressed by explaining the differences and the impact in general terms.
C1Q3	In normal circumstances, we believe that it is appropriate for a financial adviser to provide information on costs for items 1, 2 and 6 in Table 4. With respect to item 3, there are a range of different reasons why an SMSF might be wound up or why an individual may leave the fund. Costing these different scenarios is problematic. The requirement would need to be more specific. In terms of item 4, this remains a complex matter as it is dependent upon the level of activity that the trustees wish to take on, versus what they outsource. It also depends upon the number of members in the fund, including expected future members. We believe that this is better addressed in terms of general guidance rather than specific points or asset levels. As stated above, we do not believe that it is practical to provide time costs associated with managing an SMSF. It is certainly appropriate to express this in terms of a likely range of hours per year, but converting this to a specific cost is problematic. Different people will place different values on the time that they devote to their SMSF.
C1Q4	We are not aware of any other key costs that should be included. Any disclosures should be in terms of a range of costs.
C1Q5	We do not believe that any other disclosures about costs are required.
C1Q6	Yes there will be additional costs that flow from these requirements, including additional software requirements, potentially changes to SoA templates, process changes and

Question	Response
	training of financial advisers. We are unable to calculate these costs or present them as figures. There will be costs at the licensee level and at the adviser level, thus the cost per adviser will vary depending upon the number of advisers in the licensee.
C1Q7	We have identified the issues above where we believe there will be practical problems in complying with these obligations.

Conclusion

We thank you for the opportunity to provide feedback on the proposal with respect to disclosure requirements for SMSFs. In our view these proposals are important and are largely supported in terms of intent. We believe that they can be implemented through regulatory guidance rather than a Class Order and we also propose that they are done as much as possible through stand-alone documents rather than changes to SoA templates. We believe that it is necessary to ensure that the balance is right across all these requirements, to ensure that there is sufficient value for clients to warrant the extra effort and cost involved.

Should you have any questions, please do not hesitate to contact me on 02 - 9267 4003.

Yours sincerely,

Philip Anderson

Chief Operating Officer