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**Institute of
Chartered Accountants
Australia**

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Dear Ai-Lin,

Consultation Paper 216 – Advice on SMSFs: Specific disclosure requirements and SMSF costs

The Institute of Chartered Accountants in Australia (the Institute) would like to take this opportunity to make the following comments in relation to the development of ASIC's proposals on specific disclosure requirements and SMSF costs.

The Institute is the professional body for Chartered Accountants in Australia and members operating throughout the world.

Representing more than 73,000 current and future professionals and business leaders, the Institute has a pivotal role in upholding financial integrity in society. Members strive to uphold the profession's commitment to ethics and quality in everything they do, alongside an unwavering dedication to act in the public interest.

Chartered Accountants hold diverse positions across the business community, as well as in professional services, government, not-for-profit, education and academia. The leadership and business acumen of members underpin the Institute's deep knowledge base in a broad range of policy areas impacting the Australian economy and domestic and international capital markets.

The Institute of Chartered Accountants Australia was established by Royal Charter in 1928 and today has more than 61,000 members and 12,000 talented graduates working and undertaking the Chartered Accountants Program.

The Institute is a founding member of both the Global Accounting Alliance (GAA), which is an international coalition of accounting bodies and an 800,000-strong network of professionals and leaders worldwide; and Chartered Accountants Worldwide, which brings together leading Institutes of Chartered Accountants in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support, develop and promote over 320,000 Chartered Accountants in more than 180 countries around the world.

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If you have any questions regarding our submission, please do not hesitate to contact me

Yours sincerely,

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General comments

The Institute broadly supports measures that will enhance the quality of information that is given and available to existing and potential SMSF trustees. With \$500 billion currently being held in the growing SMSF sector, the Institute understands the focus being directed towards it by ASIC and the government.

While we appreciate that ASIC's responsibilities are with regard to advice provided by those that are or should be operating under an Australian Financial Services Licence, we believe that the type of information contained in disclosures addressed in the consultation paper should be made available more broadly and that ASIC has an opportunity to work with other regulators and the superannuation industry to ensure all potential SMSF trustees are made aware of various issues prior to setting up an SMSF. As advice is not a requirement for those considering an SMSF we must ensure that anyone, regardless of whether they seek professional advice or not, are aware of certain issues and considerations prior to setting up an SMSF. This process therefore needs a more educational approach for all potential SMSF trustees rather than a compliance approach for advisers.

We believe the greater risk of awareness of the responsibilities for potential SMSF trustees lies not with the provision of advice from financial advisers and professionals but with those who are not seeking any advice or are receiving advice from non-professional and unregulated sources, including family or friends. The question must be asked as to whether the proposed measures in the consultation paper are too narrowly focused in the wrong area.

The Institute encourages further consideration as to whether the specific disclosures proposed by ASIC are warranted or whether they are adequately covered by provisions under the Future of Financial Advice best interests duty. We caution whether further disclosure requirements should be implemented now at a time when new requirements under best interests duty are still being bedded down.

Furthermore, we caution that the proposed requirements appear to respond to issues that are not systemic in nature. Whilst ASIC's findings in its recent review of SMSF advice (REP 337) noted that there was room for improvement in some areas, most advice was found to be adequate. This is despite the fact that the pieces of advice being reviewed were considered to be high risk. We would encourage appropriate consideration before further layers of compliance are pushed onto advisers.

The Institute would also encourage consideration as to if and how existing SMSF trustees should be made aware of certain information contained in the proposed disclosures. With 500,000 funds already holding \$500 billion in assets, it may be similarly important that these trustees are informed about certain issues, such as the operation of the statutory compensation scheme.

Specific comments

Proposed Disclosure Requirements

B1 Warnings about lack of statutory compensation for SMSFs

While we do not specifically oppose the inclusion of a disclosure within the body of a Statement of Advice, it should be noted that warnings in relation to the lack of access to a statutory compensation scheme already exist within the ATO's trustee declaration form. Notwithstanding that we believe the processes and timing of the signing of this form be amended (see below), it is important that duplication of information to trustees does not ultimately discourage them from reading any of the information and disclosures provided. The volume of information can be overwhelming and have the reverse effect to that intended. We therefore caution that proceeding with the inclusion of this disclosure may not achieve its objective.

Ensuring awareness of all SMSF trustees

All new SMSF trustees, regardless of whether they are setting up a new fund or joining an existing fund are required to sign the ATO's trustee declaration form. This document outlines trustee responsibilities and obligations in running an SMSF and additionally includes statements regarding the lack of access to a statutory compensation scheme. We believe that a more appropriate process to ensure potential trustees are better informed about these measures is to address the timing, content and processes around signing this form.

One of the major shortcomings of the declaration is that the form is not required to be signed prior to setting up the fund. It is only required to be signed within 28 days of becoming a trustee. It is however reviewed by SMSF auditors as part of the first year audit. While the Institute believes the warning in the current form regarding the statutory compensation scheme can be justified, the timing of the declaration means that most funds may have already been set up by the time the trustees are made aware of the relevant information.

We would strongly encourage ASIC to work with the ATO to require the declaration to be signed at the point at which a trustee applies to set up a regulated super fund. This could be achieved by including the declaration in the initial application form to become a regulated fund. This would achieve the following objectives:

- Ensure all trustees, regardless of whether they receive professional advice are made aware of the operation of the statutory compensation scheme.
- Awareness of the scheme and other trustee responsibilities and obligations is achieved before an SMSF is set up.
- The ATO will have better oversight over the signing of the declaration as it is physically provided to them with the initial application form.

We also believe that bolstering the mechanisms and wording of the trustee declaration form will be beneficial for all potential SMSF trustees, not simply those that have received financial advice.

Prescribed format

Should ASIC proceed with requirements for statutory compensation disclosures, the Institute supports the provision of a prescribed format as to how information around the lack of access of SMSFs to a statutory compensation scheme is provided.

We believe however that the wording needs to educate potential trustees, not simply 'warn' them. An inability of SMSF trustees to not access such a scheme may not necessarily be seen as a negative feature, particularly in relation to fees that may otherwise apply. If the investor has invested in low risk assets with large reputable organizations (for example, direct investment in a diversified portfolio of blue chip stocks) the lack of access to a scheme may be of little consequence.

We note comments made by SMSF investors following the Trio inquiry that even if they had known about the lack of access to a scheme, it would not have made any difference to their decision regarding setting up an SMSF or investing through Trio as they believed APRA and ASIC had oversight over Trio and their financial adviser.

Furthermore, disclosures must address the true operation of the scheme, including how members of APRA regulated funds are affected.

Broader disclosures about the operation of statutory compensation schemes

We believe that if it be deemed appropriate to include specific disclosures on statutory compensation schemes for SMSFs then it is warranted that similar disclosure of the operation of the statutory compensation scheme for all other types of funds should also be included.

It is not appropriate to 'warn' SMSF trustees about the lack of access to a statutory compensation scheme without discussion on how the scheme applies to other types of superannuation funds. In order to provide a balanced, educational and useful disclosure, potential trustees should also need to understand that being a member of an APRA regulated fund does not guarantee that they will be covered under the scheme in the event of a fraud. In addition that specific approval needs to be provided by the relevant Minister before access is granted.

Furthermore, compensation amounts are still ultimately paid by the members of superannuation funds via a special levy.

The disclosure must not imply, (by omission or overtly), that being in another type of superannuation fund guarantees coverage under the scheme or that there is no cost associated with compensation being paid out. Importantly, members of larger funds may incur costs associated with the scheme regardless of whether they are directly impacted by a fraud.

Separate declaration

We do not believe that SMSF trustees should be required to sign a separate document with regard to the statutory compensation scheme. This is already appropriately included in the ATO trustee declaration form.

Burden on advisers to include in Statement of Advice (SOA)

We believe the burden on advisers to include such a disclosure would not be excessive. However we caution that the cumulative effect of additional disclosures can impact the overall provision of advice. It is well accepted that large amounts of disclosures contained in extensive Statements of Advice are frequently ignored or unread by the recipients of advice.

It remains a challenge to ensure that SOAs are well balanced with appropriate information but not overloaded with disclosures that clients are unlikely to read.

B2 Disclosure Requirements

Broadly speaking, the Institute believes that much of these disclosures require rewording to appropriately deliver the objectives ASIC is endeavouring to achieve. We are concerned that the current wording implies a negative connotation rather than simply providing education for trustees about some of the specific requirements of running an SMSF and the relative merits in comparison with larger APRA regulated funds. This information should be in a form to allow trustees to properly understand and make an informed decision in regards to an SMSF. It is not appropriate to treat these disclosures as warnings about SMSFs, particularly when there are also risks and considerations for all types of funds.

We believe that, as discussed above, inclusion in the existing (or amended) ATO trustee declaration form may be a more appropriate way of conveying information to trustees. Again, we would strongly encourage ASIC to work with the ATO to enhance the timing and processes around the trustee declaration form to achieve a better outcome for all SMSF trustees, regardless of whether professional advice is received.

We are also very mindful of ASIC's position in ensuring disclosure is "clear, concise and effective". This has recently been reiterated in the latest updated ASIC RG 175

Notwithstanding, we believe a better process is available for the provision of information to trustees, we make the following comments in relation to proposed disclosures contained in the consultation paper.

Item 1 Responsibilities and obligations for SMSF trustees associated with running an SMSF

Without being overly prescriptive, it will be important to provide guidance to advisers on the scope of responsibilities and obligations that ASIC would expect to be provided to potential SMSF trustees. Realistically, the full extent of trustee responsibilities extends to vast amounts of detailed legislation and regulation which practically cannot be conveyed to them. Alignment with the trustee declaration form would be warranted to cover the major issues for consideration by trustees in running an SMSF.

General statements requiring explanations of responsibilities and obligations of trustees may leave an adviser exposed if they have not disclosed a minor issue that ultimately impacts on an SMSF trustee at a later date.

The inclusion of commentary that a trustee's responsibilities remain with them, regardless of the use of service providers such as administrators, advisers or tax agents is warranted. Additionally, raising awareness of shared responsibility by trustees regardless of a dominant trustee is appropriate.

Item 2 Risks associated with an SMSF

Lack of insurance – we believe the rewording of this section would be required. The Institute is concerned that the current wording implies inaccuracies as to how insurance operates within APRA regulated funds.

It must be clear that insurance in APRA funds is not always automatic. Additionally, insurance coverage in an APRA fund may be grossly inadequate for an individual and it does come at a cost. If the disclosure is designed to address specific issues with an SMSF, it must not imply that APRA regulated funds are the 'answer' to perceived shortcomings. The risk is that a potential trustee may make a decision to remain with an APRA fund under a misapprehension as to how insurance may apply to them.

The disclosure must also be clear that insurance is still available within an SMSF, albeit not automatic.

While insurance should be considered in any decision to switch from an APRA fund to an SMSF, a balanced disclosure is vital to ensure that potential trustees are making a fully informed decision.

Other risks – While there are considerations that need to be undertaken when assessing whether or not an SMSF is appropriate or not, these should not be labeled as 'risks'. Again, the Institute would strongly encourage re-wording of proposed disclosures to accommodate a more educational approach to the provision of information. For example, while it is true that SMSF trustees do not have access to the Superannuation Complaints Tribunal, this may not necessarily be considered to be a risk. Furthermore, the operation of SCT for members of APRA funds may be perceived as coming with its own risks. The use of individual trustees does not necessarily constitute a risk for trustees either. Corporate trustees are generally considered to be administratively easier and may have certain advantages but this does not mean individual trustees are risky.

A table of advantages/disadvantages may be more appropriate or simply a list of considerations in a factual/educational manner. We would encourage further consultation with industry on the major issues that should be included in this section.

Item 3 The need to develop and implement an appropriate investment strategy for an SMSF

While SMSF trustees are required to develop and give effect to an investment strategy for their fund, the wording of this disclosure does not appropriately reflect the requirements. The use of the word 'appropriate' is highly subjective and not a legal requirement. Trustees are required to *consider* a number of factors in designing their strategy.

The statements that an investment strategy "ensures the fund is likely to meet the members' retirement needs" is inappropriate. It implies that the SMSF is the only retirement savings that a person has, that they know at the time what their retirement needs will be and fails to address legal barriers to achieving this objective (eg maximum contribution levels).

We would encourage the wording to better reflect legislative requirements regarding creation and review of investment strategies and alignment with guidance from the ATO.

Item 4 The time commitment and skills needed to run an SMSF effectively

This disclosure is in part already addressed in Item 1. It may be more appropriate to build on wording contained in Item 1 to address the time commitment required by trustees to run their own fund. Again, we encourage an educative approach to the wording rather than implying risk. Statements to the effect of tailoring a trustee's time commitment based on the level to which they intend to outsource certain operational functions is warranted.

Item 5 The costs of managing an SMSF

While costs of managing an SMSF are an important consideration by potential trustees, re-wording is required for this section to give a more balanced assessment of costs in both SMSFs and APRA funds.

It should also be clear that the provision of estimates for costs can be extremely difficult where other external service providers may (or may not) be involved. There can be a large difference in what administrators, tax agents, actuaries, auditors and accountants charge, depending on the level of service provided as well as other considerations. The choice of these providers may be at the discretion of the client and well outside the control of the adviser.

The provision of estimates based on any number of scenarios may result in large amounts of disclosure which ultimately may be overlooked. To the extent that an adviser can provide estimates, they should. However a statement encouraging trustees to make their own enquiries about costs from their other service providers would be appropriate.

Item 6 The need to consider and develop an exit strategy for an SMSF

The Institute does not believe that this disclosure accurately reflects legal obligations associated with running a fund. The wording implies that trustees must develop such an exit strategy.

While awareness of the possible need to exit an SMSF may provide some value to trustees, the disclosure must not be seen to mislead trustees as to their obligations but provide meaningful information. It would be useful to provide trustees with reasons why a need might exist to have an exit strategy but in an informative, educational and awareness based manner.

It may not be appropriate to develop an exit strategy for the fund or its members at the time of setup as it would not be possible to develop an exit strategy for the vast array of scenarios which may arise that would warrant exiting a fund. Arguably, a number of these scenarios will be ignored by trustees as impossible (eg divorce is not a scenario generally considered by happily married couples). It should be noted also that the same consideration may need to be given to scenarios within larger funds.

Item 7 The laws and policies that affect SMSFs are subject to change

This item could be incorporated into items 1 and 2. We note however that the focus of changes in law should refer to changes in superannuation, not only SMSF law.

Transitional period

The Institute believes that, should ASIC proceed with introducing requirements for the proposed disclosures, adequate time must be given to allow system changes for providers and training for those advisers impacted by the changes. A period longer than 6 months may be required.

We would also encourage a 1 July start date as most advisers are familiar with this date as a start date for legislative changes and use the period in the lead up to this date to turn their minds to impending changes and educating themselves on all changes affecting their industry.

Early adoption by advisers and licensees should not be discouraged.

C Proposed Guidance on SMSF Costs

The Institute believes it is appropriate for information and guidance to be made available by ASIC on the costs associated with setting up and operating an SMSF, together with comparative costs associated with being a member of an APRA regulated fund.

We do not believe that this should be a mandatory disclosure for advisers but made available to potential SMSF trustees by the regulators (ASIC and ATO) including through the MoneySmart website and ATO publications.

Any provision of guidance and estimates must include statements to the effect of the variability of costs. Every SMSF will be different as to the expenses associated with running the fund with many factors contributing to the overall cost. Some fees, such as the levy imposed by the government are mandatory for all funds. Similarly, all funds will have an audit fee although this can vary significantly depending on the auditor, the nature of investments within the fund, the quantity of transactions and the complexity of the fund.

Other fees will vary significantly depending on the level of involvement by the trustees. The more engaged they are with their fund, the less likely they are to engage the services of external providers such as accountants, advisers, investment managers etc.

While indicators of costs are useful, ultimately the cost for an individual SMSF can vary considerably. We believe that advisers under best interests duty will tailor costs to their individual clients.

With regard to the proposed wording of guidance, the Institute is concerned that the language used in Table 3 of the Consultation paper is misleading. The use of the word 'value' implies that the value of operating an SMSF is based solely on cost. The value of an SMSF goes far beyond the cost of running the fund to include matters such as control and flexibility. Guidance should not promote cost as the sole or major driver of the value of an SMSF. We are also concerned that the wording contained in Table 3 does not adequately address the issue of where an SMSF may be more cost effective than an APRA fund – only that at best it would be of 'equivalent value'.