8 NOVEMBER 2013

Ai-Lin Lee
Policy Guidance Officer
Financial Advisers
Australian Securities and Investment Commission (ASIC)
GPO Box 9827
Melbourne, VIC, 3001

Dear Ai-Lin Lee,

Re: Consultation Paper 216 (CP 216): advice on self-managed superannuation funds (SMSF): specific disclosure requirements and SMSF costs

Superannuation Australia, a subsidiary of Taxpayers Australia Inc, represents both professional SMSF advisors such as accountants and financial planners as well as SMSF trustees. We are committed to maintaining a vibrant, low cost, minimally regulated SMSF sector. We are therefore interested in the proposals as set out in CP 216.

Superannuation Australia believes that the SMSF sector is currently appropriately regulated and performing well for SMSF trustees. We are not convinced of the need to massively increase the regulatory burden on the SMSF sector, particularly SMSF trustees. We are also of the view that SMSF trustees are generally very well aware of the costs of running an SMSF and actively seek to reduce those costs where they can. We are therefore not convinced that the proposals as set out in CP 216 will have much of an impact on the growth of the SMSF sector.

We do not oppose the requirement that SMSF advisers be required to disclose certain information to their prospective SMSF clients such as the fact if they set up an SMSF they will not have access to the compensation arrangements under the SIS Act. We believe that the "Best Interest" duty that is imposed on financial advisers as a result of the Future of Financial Advice (FOFA) reforms create an obligation to do so regardless of the class order.

As noted above we are not convinced that SMSF trustees are not aware of the costs of running a SMSF. In our experience SMSF trustees are very cost conscious and look to keep costs to a minimum. While there are additional costs to running a SMSF that impact on funds with low initial balances, most trustees are aware of this and have decided they would rather have the control of their investments a SMSF provides and wear the initial extra cost. However, we believe the "best interest" duty imposed on financial advisers would mandate that the adviser discuss issues such as the cost of running a fund regardless of ASIC's guidance.

Please see the material attached for our substantive submission on the issues raised in CP 216.

If you or anyone from your office would like to contact us in relation to the issues we have raised in our response to CP 216 please contact me at either or or at the address details set out below.

Warm regards

Reece Agland | Superannuation Products & Services Manager
Taxpayers Australia Inc

P 03 8851 4508 | F 03 8851 4588 | E ragland@taxpayer.com.au
1405 Burke Road | Kew East | Vic 3102 | Australia

ASIC Consultation Paper CP216: Advice on SMSF: specific disclosure requirements and SMSF costs

Disclosure Requirement

B1Q1: Do you agree with our proposed disclosure requirement in Table 1? If not, why not?

Taxpayers Australia (TAI) takes the view that the new "Best Interest" requirements under the Future of Financial Advice already create an obligation on the adviser to disclose all pertinent information to the client. When switching a client from an APRA superannuation fund to an SMSF, one of those issues to consider is the loss of the protection under Pt23 of the SIS Act that provides a compensation regime for APRA related funds but does not cover SMSF. We believe that the "Best interest" of the client is to know that they will no longer have access to the compensation scheme.

TAI supports the proposal to have a disclosure requirement. While we believe it would already be required to be disclosed due to the "best interest duty", providing a disclosure requirement will act to reinforce the best interest duty and bring it to the forefront of attention of all advisers.

TAI is also of the view that the new *APES 230 Providing Financial Advice* and the IPA's *Pronouncement 11 Providing Financial Advice*, both impose an obligation on accountants who are not currently licensed to consider the best interest of their clients. We believe to meet the requirements set out in these professional ethical standards that accountants would be obliged to explain to their client if they move to an SMSF from an APRA fund that they will lose access to the compensation arrangements set out in Pt23 of the SIS Act.

B1Q2: Do you think that the proposed warning will benefit clients who are considering setting up or switching to an SMSF?

A: TAI believes that the warning is a necessary part of any advice to set up or switch to an SMSF. Therefore, we believe it will benefit the client. However, it is one thing to bring it to the client's attention it is another to ensure that the client understands what it means and retains this knowledge.

The real issue is one of trustee education. Trustees must understand what it means not to be covered by the protection of the compensation scheme and the fact it requires them to be more diligent in checking the *bone fides* of any investment advice they receive. We believe that it would be more effective to focus on education of trustees than merely focus on the adviser end of the equation.

We don't think it will though have any impact on the decision to set up an SMSF. Most clients have already made the decision to set up an SMSF long before they have gone to their advisor. Most will have done some research and know someone who has an SMSF. Few, if any, of those who set up an SMSF have done so solely at the recommendation of their advisor without having prior consideration of doing so.

B1Q3: Do you think the proposed warning should be given in a prescribed format?

TAI does not believe the warning should be in a specific format. Advisers should be free to develop a variety of methods to inform the client. The more something becomes a standard form sentence in an SOA the less relevant it becomes and the more likely it will be ignored by the clients. Advisers should be able to recommend their trustee clients to undertake specific study or provide them with additional documentation that better spells out the trustee's obligations and requirements and issues such as the fact that by setting up an SMSF they lose access to the compensation arrangements.

We believe that advisers should be free to determine how this information is conveyed to their clients.

The problem with SOA's is that they are generally written in legal jargon to protect the adviser. This is not a good way to communicate this kind of issue to a client. While having it in the SOA is one way to achieve compliance for the adviser it may not be the most effective means of educating the client. Clients often flick through or ignore the SOA altogether.

One possibility is to get the client to sign a declaration that they are aware of their obligations and other things of importance, including the fact SMSF cannot access the compensation scheme. Such a declaration may bring the issue more front and centre to the mind of the client than having it in a SOA.

B1Q4: Do you think that clients should be asked to sign a document acknowledging that they understand that SMSF's are not entitled to receive compensations under the SIS Act?

As noted above TAI supports the idea that the client signs a declaration that they are aware of certain things. If done in the right way a declaration is an effective means of ensuring that a client considers something. It would also provide documentary evidence that the adviser has done the right thing and informed the client.

Having said that, new trustees must already provide a similar declaration to the ATO. It makes little sense to require them to sign another document similar in nature for ASIC. It would be best to modify the declaration to the ATO to include a statement they understand by setting up an SMSF they forgo the compensation under the SIS Act.

B1Q5: Are our proposed disclosure requirements likely to result in additional compliance costs for AFS licensees and their authorised representatives?

While TAI has not calculated such costs, we would be of the view that there would be some additional costs to the adviser. They would need to update checklists on what issues to raise with clients. They would have to revise SOA's and other documents to bring in line with the new requirements and they may need to develop a declaration to be signed off by the client.

While there is likely to be some costs we would not imagine they would be insurmountable or excessive.

B1Q6: Are there any practical problems with the implementation of this proposal?

We are not aware of any practical problems in implementing the proposal.

Responsibilities and risks associated with running an SMSF

B2Q1: Do you agree with our proposed disclosure requirement in Table 2? If not, why not?

As with the requirement to disclose that SMSF are not able to claim compensation like APRA funds, the disclosure requirements outlined in Table 2 should be required to be disclosed to clients as a result of the "best interest duty". Before a client establishes an SMSF they must understand the responsibilities and obligations of being an SMSF trustee. SISR 4.09 now requires that trustees consider insurance as part of their investment strategy. SIS already requires trustees have an investment strategy.

While it is worthwhile requiring advisers to disclose these issues with their clients, it is fundamentally the responsibility of the trustee to understand these and implement them appropriately. Some trustees may seek external advisers to do these things for them but many SMSF trustees take on these obligations themselves. It is therefore the trustee that needs to be the focus not just the adviser.

Clients also need to be told the cost of operating an SMSF, though this cost will vary greatly. The cost will depend on what activities the trustee outsources and what activities they take responsibility for themselves. At the moment the only requirement that must be outsourced is the audit. If the trustee does the other functions themselves then the cost of administering an SMSF will be relatively low even with small balances. ASIC must appreciate that with many SMSF set up with low initial balances, that the trustee will save costs by running the fund themselves with minimal external advice. This is the "self-managed" part of the SMSF name.

TAI questions the necessity to inform the client that the law will change from time to time. It is obvious that the law may change at any time and this may influence the client's position. Requiring an advisor to make such a statement could be considered redundant.

B2Q2: Do you think that the proposed disclosure requirements will benefit clients who are considering setting up or switching to an SMSF?

All the matters set out in Table 2 are existing obligations on trustees of an SMSF. They cannot perform their functions without being aware of these issues. The reality though is that to improve client knowledge of these requirements is not as much the responsibility of the adviser but the trustee's. It would be more effective to look at the issue of trustee education to ensure that they are aware of their obligations and take them seriously.

ASIC might be better off trying to promote trustee education tools and mandating trustee education than concentrating on the advisers. In the end it will only be a one off requirement of the adviser to inform the client of these issues, they are ongoing obligations for trustees.

B2Q3: Do you think the proposed disclosure requirements should be given in a prescribed format?

No, TAI does not support disclosure to be in a particular form. This information is likely to be difficult to properly incorporate in a SOA without it becoming another legal jargon laden series of statements in an SOA designed to merely meet the disclosure obligation rather than educate the client. It would be better if the adviser could refer the client to existing material the client can take away and read to understand better their obligations. There are many ways this information could be displayed and it makes no sense to restrict it to a bland set of paragraphs that are in every SOA and become meaningless. One option is to have a video format presentation of the client's trustee obligations. Some people retain information more easily if it is in a visual format, yet a video format would not be able to be set out in an SOA. It therefore makes sense to leave it to the adviser to determine the best means of educating the client of their trustee obligations.

B2Q4: Do you think that clients should be asked to sign a document acknowledging the responsibilities and risks associated with running an SMSF?

Trustees are already required to sign off a declaration that they understand their obligations and responsibilities as a trustee. It would not be beneficial for them to be required to sign an almost identical acknowledgement for ASIC purposes. ASIC should be able to rely on the declaration provided to the ATO. If necessary changes could be made to the ATO declaration, rather than require trustees sign off another declaration.

B2Q5: Are our proposed disclosure requirements likely to result in additional compliance costs for AFS licensees and their authorised representatives?

Given the complexity of the issues involved with these additional disclosure requirements there is likely to be considerable extra costs to AFS licensees and their authorised representative. Advisers will need to be trained in understanding these disclosures and explaining them to their client. While accountants have had years of experience doing this, it may be new requirements for advisers. Documents will need to be developed to inform clients of these requirements. However, if advisers are able to rely on third party providers of this information they could do so using existing materials developed by groups such as Taxpayers Australia. This would drastically reduce the cost to the licensee and authorised representatives.

However, we believe that the "best interest duty" would already impose an obligation to discuss these issues, and therefore requiring it to specifically set out in a class order should not impose too much additional cost than "best interest duty" would already require.

B2Q6: Are there any practical problems with the implementation of this proposal?

We are not aware of any practical problems in implementing the proposal.

B2Q7: Do you think we should provide further guidance on the disclosure obligations?

No.

B3Q1: Do you agree with the proposed timeframe for the implementation of proposals B1 and B2?

Six months should be sufficient for firms to update their manuals and systems to take into account the proposed requirements. The requirements should only apply to new clients and not existing SMSF clients.

Rice Warner findings on costs of administering an SMSF

C1Q1: Do you agree with Rice Warner's findings?

The costs of running an SMSF will vary enormously and are nearly impossible to compare with an APRA superannuation fund. At the simple end of the SMSF range you have an SMSF in pension phase drawing down an allocated pension which will have very little ongoing costs of administration all the way up to a complex SMSF with borrowings, a variety of investments including collectibles where the management of the fund is outsourced to a commercial corporate trustee. He costs of each are not comparable to the other.

It is clear that the smaller the balance the higher the cost ratio of running the fund is. But it is also true that many small funds will have simple investment strategies where the investments and day to day running of the fund is by the trustee. If they do all the work themselves then the only external cost (other than time) will be the audit, the annual ATO advisory fee and maybe some administration software. With simple audit starting around $350 p.a. it can be quite cost effective for a person to manage their own fund.

The Rice Warner numbers are based on the proposition that the fund has a corporate trustee and has their tax affairs done externally. While it is recommended that an SMSF use a tax agent to prepare their accounts, there is nothing stopping a fund from doing the return themselves. In a very simple fund this could reduce the costs as proposed by Rice Warner from $1,163 to $500.

So a fund with say $100,000 in investments, they are invested in a few blue chip stocks and some money in a term deposit. The Trustee does the investments and takes on all the administration and even does the funds tax return. The only costs are an audit at $350, software at $150 and $100 in ancillary costs. On top of this is cost of ATO advisory fee of say $200. Thus the cost of administering the fund is $800 for the year, or 0.8% of the fund's assets.

Compare this to a fund of $300,000 that uses an external administrator who also handles the tax return and independent auditor for $3500 per year. Also due to the complexity of their investment and need to change the trust deed they had ancillary cost of $500. Plus annual ATO supervision levy of $200. That would make the cost of running the fund $4200 or 1.4%.

In the examples above it is clearly cost effective to run an SMSF with low balances

It is where the investments get more complicated or where more work is outsourced that the costs begin to rise. However, this is usually more prevalent in SMSF with higher balances.

Therefore it is not possible to say that a fund with small uncomplicated investments is relatively more expensive to run than a higher balance fund with complex structures and investments.

In the end it all comes down to how much the trustees can and are willing to take on themselves. They are called "self-managed" for a reason, many choose to manage their fund themselves and therefore avoid the high costs of administration and investment advice.

C1Q2: Do you agree that we should provide guidance on the costs associated with setting up, managing and winding up an SMSF?

Generic guidance is going to be of little value to trustees of SMSF. Each SMSF will be different to administer depending on what work is outsourced, what types of investments are made, and how difficult the audit is. Therefore the costs are likely to vary widely.

a) The costs associated with setting up an SMSF include, cost of getting a trust deed, cost of setting up a bank account and rolling over existing superannuation into the SMSF. You may but do not need a financial adviser or accountant to help you set up the fund. Costs of this will vary depending on the complexity of the SMSF. The only necessary cost of running a SMSF is the audit, but this can be as low as $350. The fund also must pay the annual ATO supervisory fee. All other additional expenses depend on the fund in question. They may have but don't need a tax agent to prepare the taxes, a financial adviser to advise on investments, an administrator to administer the fund, software, legal costs for changing a deed and other ancillary administration costs.
b) There are many issues to consider when having insurance in your SMSF. The main considerations are whether you have insurance existing already either in another fund or outside of superannuation. It may pay to keep some money in an existing fund to get access to group insurance at discounted rates. You can still establish the SMSF just not transfer all the funds over. Also some kinds of insurance don't work in a SMSF such as "own occupation" TPD insurance. It may also be difficult to transfer insurance in your name into the SMSF funds name, this may be extinguishing one insurance starting another. This can be expensive and may result in new waiting periods or non-cover for existing injuries. There may be very good reasons not to put your life and TPD insurance in your SMSF.
c) No we do not believe it is possible to put fixed dollar amounts on these costs. While it may be possible to put a "ball park" range for the cost of setting up an SMSF, the costs of day to day management will vary so considerably as to make a price range useless. Insurance will not be possible to assess the cost without doing a full analysis of their current situation, what type of insurance and how much they need. A ball park figure might be possible.

Therefore, we believe it will be difficult if not impossible to give too much guidance on how much it will cost to run an individual fund. At best advisors could talk about the different costs that might be incurred and give some general information about how much it might cost to run an SMSF but in the end the individual costs is likely to be ascertainable without knowing how much work the trustees take on themselves and how much they choose to outsource.

In the end we do not believe these requirements will have much of an impact on the decision making of those who are deciding to set up an SMSF. They have generally decided to do so before talking to their advisor and in many cases are very well aware of the costs of running an SMSF. Of those who set up an SMSF with low initial balances generally appreciate that in the early years this may be more costly than other superannuation options but are willing to wear that cost for the control they gain over the SMSF and the expectation that over time they will raise their fund from a low balance fund to a high balance fund and thus have a generally lower cost of administration than retail or industry fund options over their whole life.

If ASIC is seeking to change member behaviour away from setting up an SMSF we believe the effort will be futile. If ASIC is seeking to show advisors how they can minimise their risk, then the proposals may have some validity.