Attachment to Information Sheet 274

Example case studies: Advice on the suitability of a self-managed superannuation fund

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The Australian Securities and Investments Commission (ASIC) has prepared two example case studies to demonstrate that the starting balance of a self-managed superannuation fund (SMSF) is one of a range of factors a financial adviser should consider when determining the suitability of an SMSF for their client.

As outlined in ASIC's Information Sheet 274 *Tips for giving self-managed superannuation fund advice* (INFO 274), there may be circumstances where an SMSF with a low starting balance is consistent with the client's best interests. There will also be circumstances when an SMSF with a higher starting balance is not in the client's best interests because it does not meet the client's objectives, financial situation or needs. For example, the client may not have the skills, time or experience to adequately carry out the duties of a trustee.

> **Compliance tip:** There is no 'one size fits all' approach to determining whether an SMSF is suitable for a client. Financial advisers should use their professional judgement and consider their client's relevant circumstances when determining whether an SMSF is suitable for their client. The client's superannuation balance is one of several factors that may make the SMSF suitable as explained in these examples.

Example 1A: Superannuation balance of $172,000 (SMSF may be suitable)

Background

The clients, Lauren and Chen-Xi, have been thinking about how to continue building their wealth. Five years ago, based on advice from their financial adviser, Roger Fore of ABC Advice Pty Ltd, Lauren and Chen-Xi used an inheritance to substantially reduce their mortgage and establish a personally held direct share portfolio. Lauren and Chen-Xi are actively involved and interested in this portfolio. They are both interested in investing as they work towards their long-term retirement goals. Recently, Lauren and Chen-Xi spoke with Roger about the benefits of an SMSF. Lauren's parents have an SMSF and Lauren and Chen-Xi thought that an SMSF may be suitable for them. Initially, they would like to set up another direct share portfolio within superannuation so they can play a more active role in their financial future.

Current situation

Lauren is 38 years old and married to Chen-Xi who is 35. They have no children and no plans to have children in the future. Both Lauren and Chen-Xi work in the construction industry, each earning $125,000 per year including superannuation.

Lauren and Chen-Xi live in their own home. Using their inheritance, they have reduced their mortgage and now have a balance of $15,000 outstanding. Lauren and Chen-Xi have an annual surplus cash flow of $30,000, which they have been directing into their mortgage. After setting aside a suitable cash reserve, on the advice of Roger, they now plan to redirect this surplus to increase their contributions to superannuation.

Lauren and Chen-Xi have gained investment experience through their personally held direct share portfolio. They have also sought Roger's advice on their APRA-regulated superannuation funds and investments. Through both investment portfolios they have experienced market volatility and gained an understanding of the concepts of risk and return. Lauren and Chen-Xi value Roger's knowledge and expertise and will work with Roger to continue managing their superannuation arrangements.

Lauren and Chen-Xi are in good health. They do not expect any changes to their personal circumstances.

Lauren has $90,000 in superannuation and Chen-Xi has $82,000. They both have default insurance within their superannuation fund.

Indicators that an SMSF may be suitable

Roger considered that an SMSF may be suitable for Lauren and Chen-Xi, outlining his main considerations for this conclusion:

- Lauren and Chen-Xi's goal is to continue building their wealth and understand whether an SMSF is suitable for them.
- Lauren and Chen-Xi have an interest, willingness and available time to play an active part in the management of their finances. These attributes suggest that Lauren and Chen-Xi have the potential to understand and manage their SMSF trustee responsibilities.
- Lauren and Chen-Xi understand that specialist knowledge and expertise is required to manage their diversified investment portfolio, and therefore, they may be required to engage Roger on an ongoing basis.
- Lauren and Chen-Xi have a strong surplus cash flow position.

- Lauren and Chen-Xi have demonstrated an ability to save and the intention to increase contributions to their superannuation. This means the SMSF will be cost-effective for them as their balance grows.
- Lauren and Chen-Xi's current superannuation arrangements allow them to hold direct shares. Roger compared the cost effectiveness of their current arrangements with an SMSF. As Lauren and Chen-Xi will be contributing to their SMSF, it will be cost-effective for them as their balance grows. Roger also considered Lauren and Chen-Xi's insurance arrangements and will make recommendations to ensure they are suitable for their relevant circumstances.

Example 1B: Superannuation balance of $172,000 (SMSF may not be suitable)

Background

The clients, Naira and Ted, have been speaking to a friend about the benefits of having an SMSF, including how they can use their superannuation to buy an investment property. Naira and Ted are also hoping to buy their first family home and would like advice about whether an SMSF is suitable for their circumstances. Naira and Ted sought advice from Roger Fore, a financial adviser of ABC Advice Pty Ltd, to assess whether an SMSF is suitable for them.

Current situation

Naira is 38 years old and married to Ted who is 35. They have two children aged one and three. Both Naira and Ted work in the healthcare industry, each earning $125,000 per year including superannuation.

Apart from their superannuation, Naira and Ted have no investment experience and are not interested in managing their own financial affairs. They currently find their life is very busy with their young family and they both work full time. They simply do not have the time or interest to think about investments. However, they acknowledge this may change in the future.

Naira and Ted have an annual surplus cash flow of $30,000, which they are saving for a deposit for their family home. So far, they have saved $100,000. This is Naira and Ted's primary goal that they are focused on with their young family in mind. They hope to get some family assistance to help them achieve this goal.

Ted is in good health. Naira has recently had some health concerns that are being investigated. Subject to the outcome of Naira's health concerns, they do not expect any changes to their personal circumstances.

Naira has $90,000 in superannuation and Ted has $82,000. They both have default insurance within their superannuation fund.

Indicators that an SMSF may not be suitable

Roger considered that an SMSF may not be suitable for Naira and Ted, outlining his main considerations for this conclusion:

- Naira and Ted's primary goal is to buy a property as their family home. Their surplus cash flow is directed to this goal.
- Naira and Ted would also like to understand whether an SMSF is suitable for their circumstances.
- Naira and Ted lack investment experience and interest in managing their own financial affairs as they are time poor. Currently, their spare time is fully committed to their paid employment and their young family. These attributes suggest that Naira and Ted do not currently have the potential to understand and manage the responsibilities of an SMSF trustee.
- It is important for Naira to retain her existing insurance arrangements while her health circumstances are being investigated. This may change in the future.
- The fees to set up and maintain an SMSF are not cost-effective when compared with Naira and Ted's existing superannuation arrangements and there is no indication this will change in the near term.
- Naira and Ted's current superannuation and insurance arrangements continue to be suitable considering their current relevant circumstances noted above.

Example 2A: Superannuation balance of $512,000 (SMSF may be suitable)

Background

The client, Benito, has read that an SMSF allows members to invest in a wide range of investments subject to certain trustee rules and responsibilities. During his career, Benito has been presented with investment opportunities that he supports, researches and understands. These opportunities include green energy renewables. Benito would like to consider using some of his superannuation to invest in these opportunities if possible. To find out more information about SMSFs and investment advice, Benito sought the advice of Leona Vest, a financial adviser of XYZ Advice Pty Ltd, who was referred to him by a colleague.

Current situation

Benito is 51 years old and single (divorced). He works in the power and energy industry and is earning $200,000 per year including superannuation. Benito is a long-term employee who currently has nine months’ personal leave and a combined eight months’ long service and annual leave entitlements.

Benito owns a home and recently paid off his mortgage. Benito has no financial dependants and plans to retire in 10 years’ time. With this goal in mind Benito has recently paid more attention to his superannuation fund annual statements. Benito’s primary goal is working towards a comfortable retirement and his personal circumstances allow him the time to focus on his finances.

Benito has an interest in investing after inheriting a direct share portfolio three years ago. Through his direct share portfolio and his superannuation fund, he has experienced the value of these investments rise and fall through market volatility. Benito has a particular interest in investing in the power and energy industry. He understands this industry and he can research the investments, especially green energy renewables, as he is experienced in this field.

Benito has also developed an interest in SMSFs as his brother runs his own SMSF. This has given Benito an understanding of the time commitment that is required and the responsibilities of being an SMSF trustee.

Benito has an annual surplus cash flow of $40,000 since paying off his mortgage. He is unsure of what to do with those funds and is seeking advice about this.

Benito has contacted Leona because he is aware he needs advice about whether an SMSF is suitable for him, and to fully understand his trustee responsibilities. Benito would value Leona’s knowledge and expertise about managing a diversified investment portfolio if an SMSF is suitable for him. This is because although he has some exposure to market volatility, he has not been actively investing in the direct share portfolio he has inherited. He has taken an interest in his superannuation in recent years and would now like to be more actively involved, including investing a small amount in the power and energy industry. Additionally, Benito would like advice about how to invest his surplus cash flow to maximise his retirement benefits.

Benito is in good health and does not expect any change to his personal circumstances.

Benito has $512,000 in superannuation and no insurance.

Indicators that an SMSF may be suitable

Leona considered that an SMSF may be suitable for Benito, outlining her main considerations for this conclusion:

- Benito has an interest in, and has done some research into, SMSFs. Benito is also seeking advice about whether an SMSF would be suitable for him as he works towards his primary goal of retirement in 10 years' time.
- Benito is interested in investing and has time to commit to the SMSF trustee role. These attributes are important as they suggest Benito has the potential to understand and manage his SMSF trustee responsibilities.
- Benito intends to invest some of his superannuation in the power and energy industry, especially green energy renewables, which he can research and understand, but cannot invest in through his existing superannuation fund or alternative superannuation funds considered.
- Benito understands that specialist knowledge and expertise is required to achieve a diversified portfolio, and therefore, he may be required to engage Leona on an ongoing basis.
- Benito's current superannuation balance and future contributions from his surplus cash flow make an SMSF a cost-effective solution compared to his existing superannuation fund and alternatives considered. Benito does not have existing insurance. However, Leona will consider Benito's insurance needs when providing him with advice.

Example 2B: Superannuation balance of $512,000 (SMSF may not be suitable)

Background

The clients, James and Otto, recently sold their boating business. They are looking forward to retiring in approximately 12 months when their consultancy contract with the new owners of the boating business ends. They want to know whether they have enough income in retirement and if there is anything else they should be doing to plan for their retirement. James and Otto have heard about the benefits of an SMSF, but are unsure about whether this is the right choice for them. Accordingly, they sought the advice of Leona Vest, a financial adviser of XYZ Advice Pty Ltd, who was referred to them by a friend.

Current situation

Otto is 62 years old and married to James who is 63. Both James and Otto are consultants in the boating industry, each earning $55,000 per year including superannuation. This arrangement will last until their retirement in 12 months.

James and Otto are using the proceeds from selling their boating business to extinguish debt on their family home and their holiday home by the beach. They will retain their holiday home as it generates income from short-term rentals that adequately covers the property costs and provides a retirement income stream. They have no financial dependants.

James and Otto's primary goal in retirement is to have a simpler life, free of the administration and responsibility of running their own business, which they found stressful and time consuming. They are comfortable with managing their holiday home as they don't find this stressful. They also enjoy the lifestyle benefits and income this asset provides them.

They are in good health and do not expect any change to their personal circumstances.

James and Otto have a combined amount of $512,000 in superannuation and no insurance.

Indicators that an SMSF may not be suitable

Leona considered that an SMSF may not be suitable for James and Otto, outlining her main considerations for this conclusion:

- James and Otto's aim is to understand if they have enough income in retirement, what steps they could take to plan for their retirement, and whether an SMSF is the right choice for them. Their primary goal in retirement is to have a simpler life, without the stress of running their business and to have more time to enjoy this phase of their life.
- James and Otto's boating and consulting business experience demonstrates attributes that suggest they have the potential to understand and manage their SMSF trustee responsibilities. An SMSF may also be cost-effective for James and Otto.
- Leona considered that James and Otto would find an SMSF arrangement in retirement stressful and time consuming compared to their current superannuation arrangements. This is inconsistent with their primary goal of having a simpler life at retirement.
- James and Otto's existing superannuation arrangements, if transferred to pension phase once they retire, remain suitable and cost effective. Leona considered their current relevant circumstances detailed above and suitable alternative financial products.
- Leona considered James and Otto's income from their existing superannuation arrangements and holiday property short-term rental income. This will adequately meet their retirement needs.