



File Name: 200814

Senator the Hon. Nick Sherry
Minister for Superannuation & Corporate Law
PO Box 6022
Parliament House
Canberra ACT 2600

28 April 2008

Dear Senator Sherry,

ASFA submission to the Government on the regulation of Self Managed Superannuation Funds (SMSFs)

The Association of Super Funds of Australia Ltd (ASFA) is pleased to provide the following submission to the Government on the regulation of SMSFs.

ASFA is a non-profit, non-political national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. Our members, which include corporate, public sector, industry and retail superannuation funds plus service providers who provide professional services to SMSFs, account for more than 5.7 million member accounts and over 80% of superannuation savings.

ASFA recognises that SMSFs form an important part of the Australian superannuation architecture. As such it also recognises that a majority of SMSFs are in fact run well. In the case of the SMSFs advised and/or administered by service providers that are members of ASFA, we are particularly confident that this is the case. Involvement in ASFA is, amongst other things, an indicator of a commitment to professional standards.

Nevertheless, ASFA also feels that a significant minority of SMSFs are subject to certain concerns, including lack of trustee knowledge and understanding, high fees and inappropriate investment strategies. The proper regulation of SMSFs is necessary to ensure that the public confidence in the Australian superannuation industry is not undermined or put at risk. Proper regulation also ensures the integrity of the purpose of superannuation and that tax concessions are directed at genuine retirement income savings.

Should you have any queries on the content of the submission please contact our Senior Policy Adviser, Tony Keir, on (02) 9264 9300.

Yours sincerely,

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CEO ASFA

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The Association of Superannuation Funds of Australia

Submission

ASFA submission to the Government on the regulation of Self
Managed Superannuation Funds (SMSFs)

1 May 2008

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1. Number of members in an SMSF

Issue: Is the limit of 4 members still relevant? Should there be an increase in member numbers to better reflect the changing complexity of families with break up of relationships and the blending of new families? The Joint Parliamentary Committee on Corporations and Financial Services considered an increase to 10 members as appropriate.

Current Australian Taxation Office (ATO) data shows that 89.4% of funds have 2 members or less. There appears to be no real pressure on the current restrictions with few funds today having 3 or 4 members. 4 members or less provides the opportunity for all to have a say. The larger the number of members means that there is a greater chance for all members not having a say.

Further, the role of SMSFs in the superannuation landscape is to provide flexibility for certain individuals to look after their own super or self manage - this concept should not allow more individuals to look after other peoples super unless there is a level playing field for all Superannuation trustees.

ASFA's position: ASFA does not support an increase in the limit of the number of members in SMSFs.

2. Minimum monetary limit for the establishment of an SMSF

Issue: Recent debate suggests that poor advice and aggressive marketing may be resulting in individuals establishing SMSFs without sufficient balances. Is it therefore practical or desirable to mandate a minimum viability threshold on SMSFs?

ASFA recognises that a substantial minimum amount is likely to be needed to enable the SMSF to be cost effective. However enforcing such a requirement would be difficult where extra rules would be required in regard to -

- The impact of market/ asset value changes that devalues that portfolio to below the mandated amount
- Whether the minimums apply to the whole fund or each individual member
- Where the only asset is to provide death cover only.

The concept of a minimum monetary limit is sound, but unmanageable. Based on ATO data it appears that when costs are expressed as a ratio of operating costs to total assets the ratio is smaller the greater the balance. However, it is ASFA's belief that having a substantial amount initially to be only part of the solution. Potential trustees also need a sound investment strategy and contribution plan. This would allow a balance to be built up swiftly over the first few years of the fund if the fund cannot be established with a large amount.

A related issue here is the continued prevalence of early access schemes that are being pedalled to many unsuspecting groups of individuals where the individual's account balance in a non-SMSF is small. The current modus operandi of scheme promoters sees individuals encouraged to transfer their super accounts into an SMSF from which they can access the money as they like, less a substantial commission paid to the scheme promoter. Anecdotal evidence suggests that it is mainly amounts of less than \$25,000 - sometimes representing the entire super savings of the individual - that is targeted by promoters. ASFA believes that there would be merit in stipulating that an SMSF cannot be established with a rollover from a non-SMSF of less than \$30,000 or from a figure the ATO and the Australian Securities & Investments Commission (ASIC) instructs based on the early access casework they have completed. ASFA believes that this would make it more difficult for individuals to obtain illegal access to super savings through SMSFs.

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ASFA's position: ASFA does not support a minimum monetary threshold be mandated. However, it does recommend a minimum establishment rollover of \$30,000 if the SMSF is established with a rollover from a non-SMSF.

3. Trustee Knowledge:

Issue: Is it practical or desirable to mandate minimum knowledge and propriety standards on trustees of SMSFs? Presently, there are no limitations on who can establish and operate an SMSF (other than those who are disqualified individuals). Today there is a legislative requirement for all new trustees to sign a declaration stating that they have a detailed understanding of the requirements of the SIS Act. ATO surveys of new trustees show an overall low level of knowledge of specific provisions of the SIS Act and anecdotal evidence suggests that the new trustee declaration form is not effective.

The current declaration for new trustees is seen merely as another form to fill in as reflected in the results of the ATO survey of new trustees. Minimum requirements will mean that SMSF trustees are at least in a position to manage their SMSF if they need to. Any accreditation or licence/ registration/certificate issuing process could be divested to relevant industry bodies that then may be subject to certain audit requirements by the ATO.

ASFA believes that as superannuation account balances increase so too will the attraction of SMSFs. It is in the interests of prudent retirement savings policy that trustees of SMSFs be seen to be skilled with the necessary capabilities to run their own SMSF.

ASFA's position: That trustees of SMSFs must meet certain knowledge and experience thresholds both as individuals and as a collective. These thresholds should be embodied in a special licence/ registration or certificate and should cover minimum financial literacy, investment, and legal obligations. The threshold would be achieved by completing and passing a relevant course provided by a Registered Training Organisation (RTO) or the trustee's eligibility may be certified by an independent assessor. This would be a prospective requirement and would apply to all new trustees from a certain date.

4. Penalties

Issue: The *Superannuation Industry (Supervision) Act 1993* (SISA) provides basically 2 penalty options where a breach occurs those being to make a fund non-complying (removal of tax concessions) and/or prosecution powers. Apart from these penalties the ATO also has a range of other actions it can take such as to disqualify the trustees, accept enforceable undertakings from the trustee, remove a trustee and appoint an acting trustee, freeze assets, and disqualify auditors and actuaries. This approach presents an all or nothing approach by the regulator. They are costly and time consuming.

It is important that penalties are transparent and are easily understood so that they can drive behavioural change. Explaining to a person the risk of a tax penalty being imposed is easier than explaining the risk of losing the compliance status of the fund. A sliding scale of penalties that allows the ATO to impose penalties by way of smaller amounts of fines or extra tax for minor infringements all the way to making a fund non compliant and the loss of all tax concessions is we believe more inline with modern regulation.

Part of this debate needs to also consider residency issues and the harshness of the current regime in terms of the active member test. In regards to this latter issue the globalisation of the professional workforce sees Australians working overseas for years but who always have the intention of returning to Australia.

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ASFA's position: That a flexible range of penalties be developed that provide the ATO with the ability to adequately and quickly respond to non-compliance as well as drive behavioural change.

5. Auditors

Issue: Basically an SMSF auditor needs to be a member of one of the main accounting bodies or a registered company auditor. Nowhere does it stipulate that the auditor must have superannuation knowledge nor any special audit or forensic skills. ATO compliance results are regularly showing a weakness in the quality of some auditors. To date the ATO has relied upon the standards set by the professional bodies and refers poorly performing auditors to their association for remedial and disciplinary action.

ASFA recognises that the Certified Practising Accountants of Australia (CPA), Institute of Chartered Accountants of Australia (ICAA) and the National Institute of Accountants (NIA) have recently jointly issued competency standards for their members who wish to be SMSF auditors. ASFA understands that this represents roughly 85% of all SMSF auditors currently known to the ATO. The standards come into effect from 1 July 2008.

ASFA's position: That a minimum standard or specialist category for SMSF auditors be mandated and that it recognise the need to manage potential conflicts of interest and that the skills and knowledge required are more than just those of a general accountant. The minimum standard should also require that the practitioner conduct a minimum number of SMSF audits. ASFA would support the mandating of the standards established by the major accounting professional bodies.

6. Corporate Trustees

Issue: SMSF trustees can be either incorporated or not. A corporate trustee although more expensive to establish brings with it an administrative simplicity, compared to an unincorporated trustee, especially where trustees or asset ownership changes. ASFA recognises that both forms of trustee enable the SMSF to pay pensions and both generally satisfy the rigours of running a superannuation fund. However, on balance ASFA believes that all SMSF trustees should be incorporated thus making SMSFs more accountable under the Corporations Act.

Policy Position: That a corporate trustee be mandatory for all new SMSFs.

7. Investment strategy

Issue: The current regulatory framework does not provide adequate regard to the importance of a sound and considered investment strategy. In fact the law does not specifically require an investment strategy for SMSFs to be in writing.

An investment strategy is fundamental to good governance and achieving adequate retirement outcomes. It should be a living document that is constantly reviewed and one that reflects the goals and outcomes for the SMSF and the individual members. The investment strategy for SMSFs must be created with due regard for diversity and cash flow but must also be in writing to assist trustees review whether or not they are on track to meet their retirement objectives in relation to the SMSF. However, it needs to be stated that ASFA recognises that in appropriate circumstances a single asset or asset class may be appropriate for certain individuals.

Policy Position: That it be mandated that a SMFS has a documented investment strategy (including risk and return profile) for each member within the fund and that this strategy be reviewed each year inline with the members' individual circumstances.

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8. Accountants and AFSL

Issue: 85% of new SMSF establishments are completed with the help of tax agents or accountants. There exists ample anecdotal evidence that suggests a number of individuals are being convinced to establish an SMSF inappropriately, in that the potential trustee is not fully aware of the costs and responsibilities of running their own fund.

The decision to establish or become a member of an SMSF should be done in the context of reviewing a range of superannuation options that may be appropriate. In ASFA's view Corporations Act Regulation 7.1.29 (5) as currently drafted provides a framework where all options in relation to superannuation structures do not need to be canvassed with a client. ASFA believes this may not be in the best long-term interest of the client, as there are in effect no minimum standards in relation to the advice that can be provided under the regulation. As such, the current and future needs of the client and other potential members in the SMSF are not necessarily taken into account.

Policy Position: *That the regulatory framework for any person providing a recommendation in relation to the establishment of a SMSF or becoming a member of a SMSF be subject to Australian Financial Services License (AFSL) requirements.*

9. ATO as regulator of SMSFs

Issue: The issues relating to the proper operation of a SMSF are wider than tax issues. On this basis it may be better that ASIC or APRA be the regulator.

ASFA is of the view that the ATO is the proper regulator provided that all advisers in relation to SMSFs are regulated by ASIC. ASFA is further of the view that the regulatory oversight would be improved by making it mandatory for SMSF trustees to be a corporation, thus making them more accountable under the Corporations Act. In terms of the ATO it has the ability to deal with large volumes and it is a compliance regulator and accordingly has the infrastructure to regulate SMSFs

Policy Position: *That the ATO continue to be the sole regulator in relation to compliance by SMSFs.*

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