




**COMPLIANT SMSF ADVICE –
WHAT DOES THIS LOOK LIKE?**

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#NC2020

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Christina Kalantzis is the founding Director of Alexis Compliance and Risk Solutions, a financial services compliance and risk management firm based in Sydney. She has over 20 years experience in the financial services wealth management and distribution industry and extensive risk management and compliance experience. She provides advice to ASX listed companies on Financial Services Reform (FSR) and the Future of Financial Advice Reforms (FOFA) compliance, investment and risk management issues. She was a member of the FCA treasury working committee convened by the Rudd and Gillard government throughout 2007 – 2012. She managed one of Australia's largest Financial Planning Enforceable Undertakings. She managed the first FSA Adviser banning 2005, represented Advisers in Wespole/ASIC banning hearings, was an industry expert to ASIC and the ACA as part of the Quality of Advice Survey 2002, and the FPA's head project manager for FSA, privacy and fee disclosure. She has also managed ASIC product and unit pricing breaches. Christina is a published author and speaker on compliance, corporate governance and risk management planning, her work has been published by AAMI, BMSI, Money Management, EA, Sydney Morning Herald, The Australian and the Australian Financial Review. Christina holds a Master of Laws and Legal Practice, a Masters Degree in Banking and Finance, a Bachelor of Commerce, and a Foundation Diploma in Financial Planning.

What does compliant advice look like?



Post Royal Commission and the commencement of FASEA Code – What does compliant SMSF advice look like?

- Satisfying the best interest duty;
- What are fair and reasonable fees;
- Whether the Client understands the advice; and
- Are the clients getting value from the advice?

The Regulatory Environment – Post Royal Commission



January 2020 – FASEA Code commences, 12 Standards including:

Standard 5

All advice and financial product recommendations that you give to a client must be in the best interests of the client and appropriate to the client's individual circumstances.

You must be satisfied that the client understands your advice, and the benefits, costs and risks of the financial products that you recommend, and you must have reasonable grounds to be satisfied.

Standard 7

You must satisfy yourself that any fees and charges that the client must pay to you or your principal, and any benefits that you or your principal receive, in connection with acting for the client are fair and reasonable, and represent value for money for the client.

The Regulatory Environment – Post Royal Commission



December 2019 - ATO review Audits on the top 100 SMSF auditors.

At the end of the 2018–19 financial year the ATO completed reviews on 51 of the top 100 auditors, looking at three to five SMSF audit files for each of these auditors.

The results : 10 - No further action, 36 - auditors Education outcome, 3- Voluntary deregistration , 2- ASIC referrals

..... we're concerned that some auditors failed to obtain sufficient appropriate audit evidence or failed to evaluate the evidence in order to demonstrate how the auditor arrived at their opinion on the financial and compliance audit.....

.....We're also concerned with the number of unsigned financial statements we found and the lack of other documents that should be on the audit file, such as a signed trustee representation letter, engagement letter and in some cases, a management letter

The Regulatory Environment – Post Royal Commission



October 2019 - Got an SMSF worth less than \$500k? Think again, ASIC says, Australian Financial Review, Joanna Mather, Superannuation writer, October, 11, 2019.

October 2019 - 277MR ASIC urges consumers to question whether SMSFs are right for them?

The 'red flag' indicators identified in REP 575 were:

- The client has a low superannuation balance, and would have a limited ability to make future contributions;
- the client wants to delegate all of the running of the SMSF to a paid advice-provider and/or delegate ;
- the client wants to delegate all of the investment decision making to someone else;
- the client does not have a lot of time to devote to managing their financial affairs;
- the client has little experience making investment decisions; and
- the client has a low level of financial literacy

The Regulatory Environment – Post Royal Commission



September 2019 – ATO confirmed that the 17,700 funds contacted as part of the [diversification review](#) used a limited recourse borrowing arrangement as well as having **90 per cent or more of their portfolio concentrated in one asset**

“In 99 per cent of the SMSFs contacted, the asset in question was property,” the ATO said.

The ATO also released further details of the extent of concentration risk in the SMSF market, revealing that 180,000 self-managed funds, or nearly one-third of all SMSFs, had invested 90 per cent of more of their retirement savings in a single asset or asset class.

The ATO asked trustees to review their investment strategy and clearly document the reasons behind the investment decisions.

The ATO also asked trustees to have their documentation ready for their SMSF’s approved auditor for their next audit to help the auditor form an opinion on the fund’s compliance with these requirements.

Satisfying Best Interest Duty



June 2018 - ASIC Report 575 – SMSFs: Improving the quality of advice and member experiences

In March 2017, ASIC engaged an independent expert to review 250 client files where personal advice to set up an SMSF was provided to clients by an advice provider. The client files reviewed were randomly selected by ASIC from data provided by the ATO.

ASIC staff members with the appropriate skills, training and experience also cross-reviewed 20% of the client files reviewed by the independent expert. The findings of the independent expert and the review by ASIC staff were largely consistent

Satisfying Best Interest Duty



Para 32

... In an additional 155 files (62%), we found that the advice provider did not demonstrate compliance with the best interests duty and related obligations. The fact that these files were found to be non-compliant does not mean that clients were significantly worse off as a result of following the advice or that the advice, if implemented, would result in negative outcomes. However, these files did not demonstrate that the client would be in a better position following the advice.....

Source: **June 2018 - ASIC Report 575** – SMSFs: Improving the quality of advice and member experiences

Satisfying Best Interest Duty



Para 33

.... There were two areas, in particular, that led to a client file being rated as not having demonstrated compliance with the best interests duty and related obligations—that is, where the advice provider had not demonstrated that they had:

- (a) sufficiently researched and considered the client’s existing financial products; and/or
- (b) based all judgements on the client’s relevant circumstances.

Source: **June 2018 - ASIC Report 575** – SMSFs: Improving the quality of advice and member experiences

Satisfying Best Interest Duty



Para 40. It appears that you have failed to conduct a reasonable investigation into financial products that might achieve Mr XXXX objectives and meet his needs that would reasonably be considered as relevant to advice because:

- 40.1 there is no record of product investigation on file; and
- 40.2 you failed to investigate whether IP insurance was available through Mr XXXX’s superannuation.

Satisfying Best Interest Duty



Section 961B of the Act imposes an obligation on persons who provide personal advice to a retail client to act in the best interests of the client in connection with the advice. That section, together with sections 961C, 961D and 961E, have the effect that the person satisfies the section 961B duty if the person:

- identifies the retail client’s objectives, financial situation and needs, as disclosed to the person;
- identifies and completes any reasonably apparent gaps in the information;
- conducts a reasonable investigation of potential financial products; and
- bases his or her judgements on the client’s relevant circumstances.

Satisfying Best Interest Duty



Para 253

..... In 234 (94%) of the client files reviewed, the advice provider recommended that the client switch from their existing superannuation product to an SMSF. In 204 of these files (87%), the advice provider did not comply with s961B(2)(e) of the safe harbour for the best interests duty.

Para 270

..... In 214 files (86%), we found that the advice provider appeared to have prioritised their own interests, or those of a related party of the advice provider, over the client's interests in breach of s961J. In general, the conflict of interest arose because the advice provider, or a related party of the advice provider, obtained fees or other benefits as a result of the advice provided (e.g. fees for auditing the SMSF, arranging finance for the SMSF and sourcing a property for the SMSF).

Source: **June 2018 - ASIC Report 575** – SMSFs: Improving the quality of advice and member experiences

What are fair and reasonable fees?



FASEA Code

Standard 7

You must satisfy yourself that any fees and charges that the client must pay to you or your principal, and any benefits that you or your principal receive, in connection with acting for the client are fair and reasonable, and represent value for money for the client.

What are fair and reasonable fees?



SMSF Advice and SMSF Accounting referrals

An adviser needs to consider:

- Is it in the clients interests that they receive professional accounting services in support of the recommended SMSF; Is the advisers sole benefit in referring the client to his accounting firm to share of any profits made by the accounting firm in general – and not in relation to his referral; and
- the fees charged by the accounting business are not based on the amount or volume of funds invested through the SMSF and are proportionate to the balance of the superfund; and
- The adviser has taken steps to establish the fees and charges are fair and reasonable and represent value for money for the client – by comparing them to the market for those accounting services.

What are fair and reasonable fees?

SMSF Set up costs



Para 96

.... People who were contemplating setting up an SMSF expected to pay an average of \$1,000 to set up an SMSF and \$680 per year for the ongoing administration and advice costs associated with running an SMSF. The actual cost of setting up an SMSF, however, has been estimated to range from \$916 to \$2,035.

Source: 68 ATO, *Self-managed super funds: A statistical overview 2015–16* (average expenses per fund are calculated using the median fund balance multiplied by the expense ratios for the specific period).

Source: **June 2018 - ASIC Report 575** – SMSFs: Improving the quality of advice and member experiences

What are fair and reasonable fees?

SMSF Ongoing Costs



Para 96

The average annual cost per fund of running an SMSF in 2015–16, in terms of administration and operating expenses, was \$3,595 and, for investment expenses, was \$4,173. This was up from \$3,114 and \$3,846, respectively, in 2014–15.

Source: Rice Warner Actuaries, *Cost of operating SMSFs: ASIC*, March 2013, p. 19, Table 16: Range of costs for establishment of SMSF.

Source: **June 2018 - ASIC Report 575** – SMSFs: Improving the quality of advice and member experiences

Does the Client understand the advice?



Para 6

At the very least, consumers need to understand the risks, time, resources and compliance obligations associated with setting up and running an SMSF before deciding to move their superannuation savings out of a prudentially regulated environment.

Source: **June 2018 - ASIC Report 575** – SMSFs: Improving the quality of advice and member experiences

Does the Client understand the advice?



Para 21 (e) Many members lacked a basic understanding of their SMSF and their legal obligations as SMSF trustees. For example, in the online survey:

- (i) 33% of members did not know that an SMSF must have an investment strategy;
- (ii) 30% of members had no arrangements in place for their SMSF if something happened to them;
- (iii) 29% of members thought they were entitled to compensation in the event of theft and fraud involving the SMSF; and
- (iv) 19% of members did not consider their insurance needs when setting up an SMSF.

Source: **June 2018 - ASIC Report 575** – SMSFs: Improving the quality of advice and member experiences

Does the Client understand the advice?



The SOLUTION?

Para 40 Based on the findings of our work, it is clear that:

(a) Many SMSF members do not properly understand the advantages and disadvantages associated with setting up and running an SMSF. ASIC and the ATO are further considering this finding with a view to:

- (i) enhancing current consumer and member communication material;
- (ii) further encouraging individuals to undertake SMSF trustee education; and
- (iii) providing a more tailored response to address specific knowledge gaps, by developing a way to identify individuals setting up SMSFs that may be at risk of being unaware of the obligations that come with being an SMSF trustee.

Does the Client understand the advice?



Standard 4 - You may act for a client only with the client's free, prior and informed consent. If required in the case of an existing client, the consent should be obtained as soon as practicable after this Code commences.

It is not sufficient to simply explain the effect of a recommendation to a client and gain a written authorisation to proceed.

An adviser must also be satisfied that the client understands the advisers explanation about the effect of the advice recommendations before the adviser can implement the recommendations on the clients behalf.

Does the Client understand the advice?



Standard 5

All advice and financial product recommendations that you give to a client must be in the best interests of the client and appropriate to the client's individual circumstances.

You must be satisfied that the client understands your advice, and the benefits, costs and risks of the financial products that you recommend, and you must have reasonable grounds to be satisfied.

Where the adviser is not satisfied the client understands the recommendations being made, the adviser must not proceed to implement the recommendation. To do so would breach **Standard 5**.

Are the clients getting value from the advice?



SOA and advice requirements

- You should discuss the client's superannuation balance and whether it is likely to be cost-effective for the client to set up an SMSF.
- You should discuss the likely costs associated with running an SMSF— including the set-up costs, the cost of winding up, and the ongoing costs of investment management, compliance and advice—and explain these to the client before making a recommendation to set up an SMSF. This information is contained in [INFO 206](#).
- Before recommending an SMSF, you should consider the client's ability and willingness to manage the fund and meet their trustee obligations on an ongoing basis.
- Be aware of 'red flag' indicators that may suggest an SMSF will not be suitable for a client

Record Keeping



The financial services licensee must ensure the records required to be kept by this section:

- (a) are **kept for 7 years** after the day the personal advice was provided to the client; and
- (b) are accessible by the licensee at all times during that period in a way that enables the licensee to produce the records.

This obligation continues to apply even if the financial services licensee ceases to be a financial services licensee during the period that the records are required to be kept and accessible.

Source: Class Order (CO 14/923) Record-keeping obligations for AFSI when giving personal advice

Record Keeping

Your Defence



You should clearly demonstrate in the client file the reasons or objectives that prompted the client to seek advice, and the outcomes the client wants to achieve.

This should be clear and recorded in the client's own words in the client file and in the SOA.

Disclaimer



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