

Melbourne SMSF Group
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17th July 2006

General Manager
Superannuation, Retirement and Savings Division
The Treasury
Langton Crescent
Parkes, ACT 2600

Dear Sir/Madam,

Re: Submission to improve Self Managed Superannuation Funds (SMSF)

The Melbourne SMSF Group is a non profit, self help organization providing a regular forum for exchange of information and ideas on the operation of Self Managed Superannuation Funds. The group has been operating for almost three years and in that time has grown to nearly 100 members.

The key objectives of our group are:

- Promote compliance with the SIS Act and tax legislation.
- Gain educational assistance from the Australian Tax Office and Centrelink.
- Simplify the operation of Self Managed Funds.
- Promote the preservation of retirement savings.

In the spirit of recent budget changes and the simplification of the superannuation rules, we wish to make the accompanying submission relating to Self Managed Super Funds.

We believe that suggestions made in the submission will offer significant advantages to those Australians prepared to fund themselves in retirement as well as the Government.

We would welcome the opportunity to provide further information to support our proposal, if required.

Yours faithfully,

Wolfgang J Waffler
(Secretary, SMSF Group)

Submission regarding simplification of Self Managed Superannuation Funds

1. Introduction

Many Australians fund their own retirement using superannuation savings held in ATO supervised Self Managed Superannuation Funds. These small funds are limited to four members, and typically provide income for retired individuals or couples.

Current requirements impose unnecessary cost and complexity, resulting in the need to engage expensive professionals, for no real benefit to Fund Members or The Regulator.

It is clearly in the interest of the Government to assist and encourage those funding their own retirement, especially where such assistance is non financial.

This submission presents a set of initiatives that would simplify these small superannuation funds, to the benefit of Self Funded Australians, and ultimately the Government Purse.

2. Summary of Submission

In the interest of reducing unnecessary complexity and cost for SMSFs we propose the following:

- To eliminate the requirement for the preparation of an annual audit of the records and financial statements of SMSFs.
- To eliminate the requirement for Actuary Certificates, required where a SMSF has a complying pension and the accounts are not segregated.
- To eliminate the requirement for additional Actuary Certificates for the tax exempt part, when a SMSF has a complying pension, market-linked income stream (MLIS) or Term Allocated Pension (TAP), as well as accumulation accounts.

We believe that the above requirements result in unnecessary cost and complexity, with little or no benefit to The Regulator or to Self Funded Australians

3. Details of Submission

3.1 Current Regulatory Obligations for a SMSF

Under superannuation law, the trustee of a SMSF is required to comply with significant regulation, including the following:

- Administration of the fund in compliance with the SIS Act, SIS Regulations, and other tax law.
- Operation of the fund in full compliance with the fund's Trust Deed.
- Preparation of detailed Administrative Records for the fund.
- Preparation of detailed and assessable Accounting Records.

- Preparation of an annual Operating Statement and Statement of Financial Position for the fund.
- Annual lodgement of a combined income tax and regulatory return, Member Contributions Statement, and a number of other reports, to the Tax Office.
- Audit of all fund records, accounts and financial statements of the fund, each year, by an approved auditor.
- Provision of a Complying Certificate for complying pensions by a certified actuary.
- Provision of Tax Certificates by a certified actuary (for exempt current pension income) for funds that have a mixture of liabilities for pension and accumulation phases.
- Preparation of and compliance with the fund's Investment Strategy.
- Retention of fund records in accordance with the requirements of the SIS act and the ATO.

While we recognise the need for sensible regulation, we can see opportunities to improve the current system and reduce unnecessary complexity and cost. These improvements relate specifically to Audit and Actuarial requirements for SMSFs.

Simplification would benefit self funded Australians, at no cost to the government, and would help to extend savings and ultimately reduce any later need for government financial support.

3.2 Issues Relating to Audits

The obligation to conduct an annual independent audit for a small SMSF adds cost and complexity, and offers little or no benefit to Self funded retirees, or the ATO. We believe that the audit requirement should be discontinued for the following reasons:

- Annual audits appear to be an excessive requirement for such small entities, generally holding retirement savings for an individual, or husband and wife.
- Similar entities including Private Companies, Private Trusts, Partnerships and Individuals, are not required to have their accounts audited annually.
- Auditors take no responsibility for the fund's compliance with regulations, or deliberate abuse of rules. Audit reports typically state that:

“The fund's trustee is responsible for the financial report and ensuring compliance with the requirements of the SIS Act and SIS Regulations”, and

“Because of the test nature and other inherent limitations of an audit, together with the inherent limitations of any system of internal control, there is an unavoidable risk that some material misstatement, fraud or irregularity will remain undiscovered”.

Audits offer little value to the Fund, because the Trustee still remains solely responsible for compliance and for the accuracy of all fund records and reports.

- Audits are not needed to protect the interests of SMSF Members. Members must also be Trustees and are unlikely to act against their own best interests.
- The ATO, as Regulator, has a number of very helpful and effective checks and balances, and also currently conducts about 3,600 audits of SMSFs per annum. (Speech by Michael D'Ascenzo, Commissioner of Taxation, 1st March 2006, Sydney).

- Audits add to the already significant annual compliance costs for SMSFs, and erode the savings of self funded retirees, potentially resulting in their earlier dependence on government support.

3.3 Issues Relating to Actuary Certificates

The requirement to obtain Actuary Certificates for each SMSF pension stream also involves unnecessary complexity and cost, and offers little or no benefit to self funded retirees or the ATO. We believe actuary requirements should be discontinued for the following reasons:

- The requirement for Trustees to maintain accurate records of the value of pension entitlements for each member is not diminished, and compliance can be verified at any time by ATO Audit.
- Actuary Certificates are not needed to protect the interests of SMSF Members. The Fund Trustees are also members and as such have no reason to deprive themselves of pension entitlements.
- The Actuary Certificate is simply a reflection of information which has already been established and provided by the Trustee, and as such provides no real new information.
- The ongoing longevity and sustainability of a pension depends on the performance of investments chosen by The Trustees. The existence of an Actuary Certificate in no way guarantees the performance of these investments.
- Regulatory involvement which limits investment choice to low return options may well result in detrimental outcomes for self funded Australians.
- Actuary Reports and Certificates also add to the already significant annual compliance costs for SMSFs, and erode the savings of self funded retirees, potentially resulting in their earlier dependence on government support.

4. Long term Impact of ongoing costs

4.1 Basic Compliance Costs

For the purpose of later discussion, we estimate the basic annual compliance costs for the running of a Self Managed Fund to be as follows:

	Accumulation Phase (\$ Cost Range)	Pension Phase (\$ Cost Range)
Accounting	1,000 - 3,000	1,000 - 3,000
Audit	300 - 600	300 - 600
Tax and Reg. Return	200 - 400	200 - 400
Actuary Certificate (ea)	0 - 0	400 - 500
Complying Certificate (ea)	0 - 0	200 - 400
Totals	\$1,500 - \$4,000	\$2,100 - \$4,900

4.2 Long term impact on retirement savings

Ongoing annual regulatory costs can seriously impact on retirement savings. It is not only the impact of the leakage of capital, but also the cumulative loss of earnings this lost capital would have provided.

A couple with a pension stream for each person from unsegregated assets would both require Actuary Certificates costing \$400 to \$500 each. If Complying Certificates are also required for exempt income at a cost of \$200 to \$400 each, the total Actuarial charges would be between \$1,200 and \$1,800 per annum. In addition, Audit costs would add a further \$300 to \$600 per annum.

An average figure for the Audit and Actuary costs referred to in the above case would be \$1,950 per annum.

If the effect of these costs is modelled from age 60 to age 85, and allowance is made for the loss of earnings on these amounts, the total cumulative cost totals \$117,000. This is the real amount in today's dollars and assumes a very conservative real earnings rate (above inflation) of 6% per annum. This represents a significant erosion of retirement savings.

4.3 Overall impact on national SMSF retirement savings

There are currently 300,000 plus SMSFs operating in Australia. At an average audit cost of \$450, this represents a loss of \$ 135Million per annum, for audit costs alone.

We do not know the number of funds running pension streams, or how many Actuary Certificates are issued, but we believe that Actuary costs would substantially increase the above figure.

We also believe that over time Centrelink must be ultimately make up for much of this loss as retirement savings are eroded.

5. Summary

In summary we believe that current requirements relating to Audits and Actuary Certificates offer little or no value for Self Funded Australians or The Regulator, and result in a significant cost impact on savings, and eventually the Government Purse.

We therefore recommend that this issue be given serious consideration as part of the current effort to simplify and improve the Superannuation System.

Wolfgang J. Waffler (Secretary),

on behalf of The Melbourne SMSF Group