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Division Head
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

To Whom it may concern

Re: Three-yearly cycle for some self-managed superannuation funds (Treasury submission)

The Guardian 16 April 2018

> **The deputy chair of the Australian Securities and Investments Commission, Peter Kell, told the banking royal commission that ASIC did not believe the financial advice industry was a 'profession'.**
>
> **Australia's corporate regulator has revealed 90% of financial advisers who provide advice to self-managed super funds have failed to comply with the best interests of their clients.**

In view of this failure outlined by ASIC's Peter Kell, is it a bad joke that Treasury proposes a three-year audit cycle?

The proposed measure for a three-year audit cycle focuses on reducing the cost of the audit process. However, we believe there are greater costs associated with the risk of not having an annual audit. The recent trend shows the risk levels faced by the trustees are rapidly rising. The major risk areas are adviser fraud, elder abuse, gambling addictions and corporate fraud as revealed in the current Banking Royal Commission.

The benefits SMSF members enjoy far out way the small cost of the annual audit rigger. Evidence from the past twenty years of annual independent SMSF audit is that it has clearly contributed to making the system stable and vibrant now and into the future.

In the words of the ATO Assistant Commissioner, Kasey McFarlane:

> *"The role of SMSF auditors and the annual independent audit that every SMSF is required to undergo are cornerstones of good governance and regulatory compliance within the sector.*
>
> *Importantly, it allows any irregularities to be identified at an early stage, thus facilitating the timely resolution and rectification of the issues by trustees."*

The SMSF audit has been designed to specifically focus on SIS compliance (refer to GS 009 AASB). However, the nation's 20 years of SMSF audits provides the empirical evidence that the annual audit has proven to act as a deterrent of systemic misbehaviour.

Some recent misbehaviour case examples are:

Example 1

Growth Plus adviser Ben Jayaweera impacted one known SMSF. The audit process quickly identified the severity of the problem. The matter was quickly referred to the authorities and three years later Mr Jayaweera has been brought to account. ASIC website states (25 May 2018).

ASIC Former Brisbane financial adviser charged with $5.9 million fraud:

- Following an ASIC investigation, former financial adviser Ben Jayaweera, of Upper Mt Gravatt, has today appeared in the Brisbane Magistrates Court charged with six counts of fraud involving approximately $5.9 million.
- The charges against Mr Jayaweera are contrary to section 408C of the *Criminal Code (Qld) and* carry a maximum penalty of up to 12 years imprisonment.

Example 2

Two separate totally unrelated funds brought to my attention. Both funds risked more than $300 000 each by the same stock broker. The audit included the review of police and court documents. ASIC website states (23 September 2016).

ASIC bans Brisbane financial adviser:

- On 26 August 2016, Mr Madhoji was sentenced to 7.5 years imprisonment with a non-parole period of 22 months in the Brisbane District court on 55 charges of fraud under sections 408C of the Queensland Criminal Code.

Example 3

The public information available on the Satvir Birk Gold Coast Adviser case should be a study for Government when considering adviser risk. ASIC website states (20 July 2017).

ASIC found that between September 2010 and October 2011, Mr Birk was dishonest in that he:

- caused cheques to be drawn on a client's superannuation account without authorisation;
- deceived some clients as to the use of funds withdrawn from their superannuation funds;
- deceived another client as to the price at which units in an unlisted registered managed investment scheme had been sold for and as to the use of the proceeds of the sale, and used a portion of the proceeds for the benefit of Mr Birk's father;

Example 4

We believe the recent outcome from the public Sherwin Securities case where bank accounts were inappropriately used, is a warning to the Government that adviser operated bank accounts are a high-risk factor and the government should put this issue at the centre of this debate. ASIC website states.

ASIC investigation

- In 2015 ASIC commenced an investigation into the operation of the Money Market Accounts held by Sherwin/DIY Super clients. ASIC's investigation related to whether two bank institutions may have processed transactions for the Sherwin Group when they should not have. The investigation into two bank institutions has concluded.

From the Australian Financial Review

- Sherwin Group collapsed in 2013, owing nearly $60 million to 400 clients.
- Adviser-operated accounts, also known as cash management accounts, allow financial advisers to monitor customers' money and make investments and payments on their behalf.
- Across the five banks there are about 530,000 customers using adviser-operated deposit accounts with balances totalling over $28 billion. A majority of customers who use such adviser-operated deposit accounts are fifty years old or older.

We believe that it should be compulsory that all banks provide for every adviser operated bank account a risk rating certificate including a fraud risk rating as part of a bank audit certificate as at the 30 June every financial year. This should be provided automatically to the trustee and to the auditor annually.

Other matters

a. Gambling addiction is fast on the rise and is having an increasing destructive effect on SMSF retirement savings.

b. Elder abuse is a major threat undermining the life savings of the elderly. 47 percent of SMSF members are over the age of 60. Please refer to the recent Attorney General Christian Porter announcement on the elder abuse matter.

c. We are now seeing for the first time widespread Superannuation Industry misconduct, as outlined by the findings of the Royal Banking Commission. The RBC lawyers are seeking to lay criminal charges on NAB and CBA.

d. Mortgage stress and the increasing cost of living is potentially relegating SIS compliance to becoming a secondary risk.

Our solution

Based on all the above, to best safe guard the community, any fund that has the following should be audited annually:

1. Funds where financial planners, stock brokers, property brokers and other adviser firms are engaged.

2. Funds that have an adviser operated bank accounts.

3. Funds that have etrade accounts and non-wrap adviser involved portfolios

It should be compulsory for all banks and investment groups to provide for every adviser operated etrade or trading account a risk rating certificate, including the fraud risk rating, as part of a bank audit certificate as at the 30 June of every financial year. This should be provided to the trustee and auditor annually.

4. Funds where they have investments and bank accounts with the investment companies named in the Royal Banking Commission.

5. Funds where they have life insurance held with the investment companies named in the Royal Banking Commission.

6. Funds where investments are managed by 100 % digital on-line platforms.

7. Funds that have an EPOA held by a child of an elderly SMSF member.

8. Funds where children act as trustee or director trustees for SMSF elderly members.

9. Funds where individuals become trustees and members to solve residency issues.

10. Funds where divorce is involved.

11. Funds with LRBA.

12. Funds with LRBA assets bought via an adviser broker system.

13. Funds with unsecured loans as assets.
Refer to the Cam and Bear Pty Ltd case.

14. Funds with secured loans to advisers such as financial and property advisers, brokers, accountants and tax agents.

15. Funds with any unlisted trust and company investments.

16. All funds in pension phase.

The three-year audit cycle is not in line with the overwhelming industry position that the current annual audit approach is optimal and that the three years audit cycle will have devastating community consequences just like the ones being revealed in the RBC. It appears the IPA, CPA, ICAA, NTAA the four largest, prominent and longest existing accounting body associations are universally of the view that they are not supportive of the three-year audit cycle. Suggesting it is more likely that there will be increased costs and no savings from the proposal.

Furthermore, the trustees of the SMSFs we come in contact with, have indicated that they prefer the SIS compliance safeguard of a yearly audit.

The logistics of the three years audit cycle is fatally flawed because accounting and administration firms are notorious for high staff turnover. The processing staff are key to ensuring that all supporting documents are gathered from the trustee for the audit. Staff in year one, year two and year three will be unconcerned with auditor's requirements and it will be the processing staff in year four that will be left ironing out the previous years of lost documents. The processing staff in the earlier years who are not trained in applying the SIS Act, and who are not required to apply the SIS Act will fail to raise the flag when there are compliance issues. However, it is the administration person in year four that will have to deal with an upset trustee and the compliance issues.

Please note the above only gets worse when the fund's administration is processed by four different administration firms. Which firms will be responsible for each audit and the provision of the relevant documents, let alone any amendments that might be required?

The Treasury has not published any evidence as to how the three years audit cycle will reduce the cost for the SMSF.

If the Government is concerned about the costs affecting SMSFs I would advise the Government to remove the $259 annual lodgement levy. It costs the six hundred thousand SMSFs around $155,400,000 annually and $466,200,000 over three years. The removal of the levy is a practical solution that would save a maximum of $777 for each fund over three years, without exposing the SMSF's to risk or additional costs. Efforts would be better off focused on reducing the mindless bureaucratic red tape that the ATO and treasury create in abundance.

Approximately 1.2 million SMSF members make up a small portion of the total superannuation membership pool. The SMSF system provides these members with privileges and benefits that far outweigh the administration and audit cost. So much so the SMSF industry continues to be one of the fastest growing sectors. The ATO statistics show that there are 36000 new SMSFs being set up annually and there is no sign of decline. This proves that thousands upon thousands of new members are driven to enjoy these great privileges and benefits. It is clear they are not deterred by the small cost of the prudent safeguard of an annual audit.

Bellas Accountants is in the top 100 SMSF audit firms nationally, based on audit volume, as advised in writing by the ATO.

My twenty-five years audit career and my life's work and expertise has been specifically focused on the audit of SMSF.

We are proud of our service record and we are proud to provide the safe guarding service to the community.

Our twenty-five years SMSF audit service history outlined above gives us cutting edge experience, visibility and the necessary understanding of contemporary risk issues facing the life savings held in SMSFs and the associated costs relating to the audit process.

Thank you for the opportunity to present this submission.

Paul Bellas
Bellas Accountants