FINANCIAL REVIEW

Future uncertain for SMSF investors

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The Coalition has promised there will be no sudden or unexpected changes to SMSF rules, but some investors are worried all the same. **Photo: Glenn Hunt**

Alexandra Cain

There has been speculation that self-managed super fund members are in the new federal government's sights, given perceptions they have access to perks other superannuation investors do not have. But so far, there are few indications as to whether SMSF members should expect changes to the way their funds are administered during the Coalition's first term in office.

Luke Lucas, principal wealth adviser at Voyager Private Wealth, says advantages SMSFs have over industry and retail funds, such as the ability to invest in direct property and borrow to invest, could be of interest to the government.

"The Reserve Bank has also started to show some concern over the use of SMSFs to invest in direct property, as there are fears starting to mount this will contribute to the next property boom. While the Abbott government has said it wants to ensure there is a 'level playing field' within the sector, it has pledged to make no unanticipated detrimental changes to the industry in its first term."

Dylan Crowe, managing director of Superannuation Property, says industry groups are asking regulators to introduce more onerous regulation over SMSF advisers.

“Regulators are attempting to ensure everyday Australians don’t get financially hurt by unlicensed operators offering SMSF advice.

“It’s easy to listen to your finance broker or local real estate agent talk about SMSFs and the rules, advantages or risks. But actually matching a client’s risk profile and financial goals to an SMSF is how everyday Australians could be misled,” says Crowe.

So far, there’s been no word on whether the previous government’s proposed tax on super fund earnings in excess of $100,000 a year will go ahead. Says Lucas: “this is particularly relevant for SMSFs where member balances tend to be higher. The ATO has also said it intends to scrutinise SMSFs more closely and to conduct more audits of SMSFs to ensure trustees are meeting all of their responsibilities and not engaging in tax-avoidance or early-release schemes.”

Brad Callaughan, director of Callaughan Partners Accountants, points out this year the ATO increased its audit activity on SMSFs from 9000 to 15,000. “We expect their activity to increase next year as well,” he says.

ASIC also involved

Phillip Osborne, member advocate at the accounting advice arm of the National Tax & Accountants’ Association, says it’s not just the ATO that has its eye on the sector. He says ASIC is paying close attention as well.

“ASIC is gearing up to take on a more proactive role in the regulation of this area. This is due to the removal of the accountants’ exemption and the fact that all advice in this area will now be regulated,” says Osborne.

The accountants’ exemption meant they could give limited advice on setting up SMSFs. From mid-2016 accountants wanting to provide advice to SMSF clients will need to be licensed or operate under another entity’s Australian Financial Services Licence. Osborne notes this will fundamentally change the advice process for many accountants and their clients.

“The other aspect that is gaining momentum in the push for more regulation is licensing of property spruikers. Direct real property is not considered to be a financial product under the Corporations Act so no licence is required for such advice,” Osborne explains.

“Since the borrowing provisions for superannuation were introduced in 2007, SMSFs have become a target for such groups and those who are unwary may not make the best investment decision. There are people with low SMSF balances that are borrowing to invest in property to boost their balances. But this may not be the right thing for them, hence the push for greater regulation in this area.”

There’s no doubt that appetite among investors for SMSFs is voracious. According to the Australian Taxation Office, from 2008 to June 2013, the number of SMSFs in Australia grew from 375,675 to 509,362. Over the last 12 months alone, the number of SMSFs has increased by 33,546 or just over 7 per cent.

Last financial year total SMSF assets exceeded $5 billion and the average fund balance is pushing $1 million, at $920,500. According to the ATO, 25.6 per cent of SMSFs have between $200,000 and $500,000 in assets. A further 23.4 per cent have between $500,000 and $1 million in assets.

The main investors

So just who is investing in SMSFs? Crowe says the main market is couples aged over 40, high-income earners and investors who are geared towards direct property rather then shares.

“Most Australians under 40 fall outside the industry guidelines for SMSF establishment,” he says.

The executive general of banking and wealth solutions at NAB, David Gall, says the initial size needed to start an SMSF has reduced in recent years.

“We used to say you needed $500,000 but now it’s more like $350,000. That is in part due to the lower costs of operating an SMSF.”

Mortgage Choice spokesperson Jessica Darnbrough says they are attractive to investors of all shapes and sizes. “A lot of small-business owners who run their businesses out of a commercial property are seeing opportunity in purchasing business premises within an SMSF. In contrast, there is an increasing number of Australians looking to purchase residential property within an SMSF.”

Darnbrough points to data from the ATO that shows the majority of SMSF members are males aged between 55 and 64. “Of all the SMSF members, 52.9 per cent are male, while 47.1 per cent are female. The majority of female SMSF members are also aged between 55 and 64.”

In terms of who is opening SMSFs, Osborne says last financial year those aged under 45 accounted for approximately 41 per cent of new SMSFs, with the 35 to 44 age group accounting for 27.6 per cent. “This puts those who are looking to accumulate benefits in the major category of new SMSF entrants,” he says.

So how do you make an SMSF a success? Osborne says the first step is to understand what you are getting yourself into. “Unless you are going to do absolutely everything yourself including tax returns, trustee minutes, deed updates, investment strategy and everything else required to ensure you meet the fund requirements, there will be costs involved to engage professionals to do this for you,” he warns.

Osborne reminds investors the penalties can be severe if the fund doesn’t meet its obligations. “So make sure you know the requirements and have a plan for how you are going to meet them.”

He says it's also essential for investors to understand why the fund is set up the way it is. "Each fund must meet the sole purpose test that requires the SMSF to be operated to meet retirement needs. Each investment that is purchased must be done with this in mind – not simply to collect various assets you want to hang on to, or to use your super balance to buy things you couldn't otherwise afford."

Advice for investors

Osborne has two tips for SMSF investors. "Have a plan that justifies why you have the fund. There is work involved and responsibilities to be taken on board, and while the rewards can be great, neglect any of these and you can severely hamper the quality of the retirement for which you are hoping."

The second tip is to work with experts. "Even though you might have your plan in place and know and understand what is required, this space has changing legislation on a regular basis. Even if your adviser is just in a mentor role to check what you are doing, it is good to have someone who works in this area to provide guidance." He says this is especially the case given the amount of legislation that is tax-related and the taxation consequences of any actions taken in relation to the fund.

For anyone who is nervous about potential changes the new government is likely to make to SMSF regulations, Wilson Pateras's SMSF expert George Pallikaris reminds investors the Coalition has stated there will be no sudden or unexpected changes for SMSFs.

"So based on that, there will perhaps be a period of stability. But the tax office is certainly devoting more resources to audit activity."

His advice to anyone considering setting up a fund is to be clear about the SMSF's investment objectives and purpose, review the fund's investment performance regularly and ensure contribution caps are not breached. He also says it's essential to make sure the fund is solvent enough to meet its liabilities and to stay up to date with changes in the law.

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