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SUPER STRATEGY NEEDS SUPER CAUTION

Recent media reports have exposed the exponential growth in the area of SMSFs. It is now such that almost all financial advisers will be working in this market. Not surprisingly, it is an area of great interest to the Australian Taxation Office (ATO), which is why it has specifically warned that “failure to comply with the [investment] rules could result in trustees being imprisoned, removed as trustees or fined, and/or the fund losing its complying status”.

So, is that all there is to cope with, ATO scrutiny? No. If you are an adviser, ASIC is concerned with how you help a client SMSF comply with one of the most fundamental rules that apply to them – documenting the investment strategy. Accordingly, financial advisers should be aware that in assisting SMSF trustees with compliance, in particular with the investment strategy, they face a real risk that needs to be managed.

We all know advisers have legal obligations to an SMSF trustee when providing assistance with the preparation of an investment strategy. But what about those advisers who provide what may be considered ‘safe standard advice’, that is, a moderate investment strategy of say 40 per cent fixed term, 50 per cent shares and 10 per cent property? Surely financial advisers cannot be held accountable for this. Right? Wrong.

INVESTMENT STRATEGY

Every SMSF must document an investment strategy. An investment

strategy details the investment objectives of the superannuation fund and the investment methods the fund will adopt to achieve its objectives. The trustee(s) of the SMSF is required to prepare and implement the investment strategy for the superannuation fund. Pursuant to s52(2)(f) of the Superannuation Industry (Supervision) Act 1993 (SIS Act) the trustee in formulating and giving effect to the investment strategy must have regard to the “whole of the circumstances of the fund”, including:

- the risks associated in making the investment and the likely returns;
- the composition of the investments as a whole, including appropriate diversification;
- liquidity of the fund’s investments; and
- the ability of the fund to discharge existing and prospective liabilities.

If the trustee breaches their obligations under the SIS Act, there a number of penalties the ATO may apply, including removing the trustee, making the fund non-compliant and even seeking civil/criminal penalties through the courts.

Given the legal obligations of trustees and the penalties associated with non-compliance, it is unsurprising trustees are seeking the guidance and assistance of their financial adviser in preparing an investment strategy. While this is all well and good, it is imperative advisers simultaneously comply

with their obligations under the Corporations Act 2001 and SIS Act to ensure they are not saving the client from the ATO only to be personally condemned by ASIC.

OBLIGATIONS OF ADVISERS

When an adviser provides assistance with the preparation of the investment strategy for an SMSF, they must, like the trustee, have regard to the “whole of the circumstances of the fund”, including the list of issues noted above. In doing so, there is the very real possibility the adviser is providing financial product advice. If this is the case and the adviser-prepared SMSF investment strategy is not provided in the form of a statement of advice (SOA), the adviser will be in breach of one of the most fundamental principles of financial planning law – giving financial product advice other than in an SOA format. They will also be at risk of losing their right to practice if ASIC takes the view that a banning order is needed, all because the adviser was helping the client to stay out of the clutches of the ATO.

Pursuant to s766B of the Corporations Act, financial product advice is a recommendation or a statement of opinion intended to influence a person in making a decision in relation to a particular product or class of financial products. In preparing an investment strategy it is nigh impossible to produce one that does not at least discuss investment classes, as well as current and future investment objectives and decisions. On its own therefore, an adviser-prepared SMSF investment strategy is perilously close to the act of providing financial product advice. In fact, because the adviser expects the

SMSF trustees to act upon it, arguably there is no real distinction with the Corporations Act requirements – the investment strategy will be financial product advice.

If this is correct, the investment strategy financial product advice must be in accordance with the requirements for the issue of an SOA. This is particularly the case as an SOA operates in a similar fashion to financial product advice – it intends to influence the recipient about certain financial matters.

So why don’t all adviser-prepared SMSF investment strategies require an SOA format? If there is a clear link between the adviser-prepared SMSF investment strategy and existing or current financial product advice that is in the lawful SOA form, the fear of an ASIC review can fall away. This is because it is not financial product advice – the SOA is, even though the adviser-prepared SMSF investment strategy talks about investment matters.

The key is to ensure the adviser-prepared SMSF investment strategy cannot be itself interpreted as investment advice for the SMSF trustees to rely upon, and this is easily achieved if it is linked to an existing SOA.

If it so happens that a financial adviser assists with the preparation of a s52(2)(f) compliant investment strategy that is not consistent with an issued SOA, then it is advisable that a statement of additional advice be provided to the client, detailing the nature of the relevant financial product advice.

The message: don’t help the client to duck the ATO investment strategy bat only to be hit by the ASIC lump of SOA wood.

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