Australian SMSF Audits

Registered SMSF Auditor
Registered Tax Agent
[redacted]

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

Dear Sir

THREE-YEAR SMSF AUDIT CYCLES PROPOSAL

I am presenting this submission to Treasury concerning the proposed changes to the SMSF audit cycle based upon my history of having nearly 30 years working in public practice, including recent years specialising in SMSF auditing.

You have raised 6 consultation questions as follows:

1. **How are audit costs and fees expected to change** – Under the current system, audit fees are under competitive stress and have had minimal change in recent year, or in some situations, have fallen. This is principally due to competitive pressures, changes in SMSF accounting packages and the introduction of electronic audit software, thus reducing audit times. While these situations are expected to continue, it is my belief as practice principal in a SMSF specialist practice the introduction of a three-year cycle will have a negative impact on fees when averaged over the 3 year cycle, based the anticipated likelihood that documentary evidence will be more difficult to locate, particularly when conducting the audit relating to a period that may have commenced nearly 4 years prior to when the audit is being undertaken. It is my belief that, when based on my practices current average fee of between $450 and $500 (plus GST) per audit, I anticipate the cost of a 3-years audit is likely to end at about $2,000 (plus GST), due to the additional time required to obtain historical documents.

2. **Definition of Clear Audit Reports** – I find the concept of clear audit reports exceptionally concerning, based on the current processes that are in place. Logic would suggest that by clear audit reports, that would suggest that the most recent audit of a SMSF's financial accounts would need to be unqualified, however, under

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the current system, that cannot be guaranteed. In undertaking the audit of a SMSF, auditors are required to form 2 opinions, firstly that the financial accounts presented represent fairly the position of the SMSF. At no point is it reported to the ATO that the auditor has issued a qualified audit in relation to the financials. The ATO will read that the fund has received a clear audit report even if the financial audit is qualified. In relation to the second opinion, where we are required to state whether the SMSF has complied in all material respects with the SISA, that can be reported to the ATO in several forms, by way of the answer of what is currently question 6 of the annual return and in specific circumstances by the lodgement of a Contravention report. Where a Contravention report is not required, the answers to question 6 is the only way the ATO will be informed of a qualified audit. That information is not submitted by the auditor, but by the trustee of the SMSF, or their authorised tax agent. Notwithstanding that the auditor is provided with a copy of the annual return, no evidence is available that the question 6 in the actual lodged return is answered correctly. It is my belief that the only solution to this would be for the auditor, in every instance, for every fund, to lodge a report to the ATO advising whether or not the audit was qualified. This could be achieved by adapting the present 'Audit Complete Advice' that is currently available within the eSat software to include additional questions, namely whether either of the audits were qualified, and further making the lodgement of the Audit Complete Advice compulsory, rather that voluntary as in the present.

3. **Definition of timely submission of SAR** – SISA s.35D states that the trustee must lodge the fund's annual return no later than the date set by the Commissioner of Taxation. Failure to do so is a breach of the SISA. In my mind, that is the timely submission. By its nature, if a trustee is granted an extension of time to lodge, that granted extension would become the date set by the Commissioner.
4. **Key events that would require an earlier audit** – The examples of key event as described in the Discussion Paper do provide a reasonable selection of possible times when an audit outside the three-year cycle would be required. The issue here, in my mind, is that by defining when the audit is required, it leaves too many holes in the planning. What if some other event occurred that was not defined, or if the definition was somewhat vague, so an argument would be presented to attempt to avoid a necessary audit. I believe a better option would be to specify the other alternative, namely, when an audit could be deferred. It may be that if a fund met specific criteria, then a deferral may be allowed. That could be that the fund had an existing pension account, only received employer contributions or similar. In effect, specific scenarios to get out of the annual audit cycle, rather than scenarios to get out of the three-year cycle. Having said that, this dos not mean I support the concept of a three-year cycle. The other issue that arises in this point is the consequences if a fund lodges an annual return without audit, when a key event has occurred. The ATO may not be aware of the key event until after the lodgement. Does the ATO then reject the annual return and instruct the trustee to have the fund audited?
5. **Transition to the three-year cycle** – There is no doubt some form of transition will be required, should the three-year cycle proceed. Personally, I see no option other than a random selection basis. The important thing is that a managed transition is required. If that does not occur, many small SMSF specific practices like mine will simply close. I will retire. Other larger practices will reduce staff and in three years there will be no suitable staff available.

6. **Other issues** – While other parties have raise some of the other issues, such as the increased risk of illegal activities, such as early release schemes, and the delay in identifying issues that may arise, I believe one vital issue that is likely to be missed is the corrective role that is currently provided by auditors. In addition to the fact that not all issues are currently reported to the ATO, the auditor can currently identify issues that have passed the accountant, or that the trustee has missed, but can be corrected prior to accounts being finalised. One example of this scenario is where a trustee may fail to fully appreciate the need to separate the SMSF from their personal affairs and pay a SMSF expense from personal funds. The ATO has confirmed that in these situations, that payment is to be treated as a contribution to the SMSF, or as an alternative where a fund is in pension mode and contributions cannot be made, it may be seen as a borrowing by the SMSF, which is a breach of the SISA. Particularly in cases where an accountant is not a specialist in the SMSF field, or where the financial accounts are prepared by the trustee, such matters can be overlooked. The auditor has the opportunity, during the process, to identify if such payments have been omitted from the financials and refer back to the accountant or trustee, allowing the financials to be corrected, thereby better reporting the member's position and possibly identifying any breaches. Such adjustment may be achievable when auditing the most recent financial accounts, but once subsequent periods have passed, this will not be possible.

Overall, while the concept of a 3-year audit cycle may sound enticing to trustees of SMSFs, I honestly believe that those trustees will be among the long-term losers. This will be of minimal benefit with a significant downside.

I trust these comments from a sole practitioner with a small practice handling around 300 audits per year will be of some benefit to the deliberations of the Department.

Yours faithfully

Eric Taylor.