

26 August 2018



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

By email: Superannuation@treasury.gov.au

RE: Feedback submission on proposed measure for three-yearly audit cycle for some self-managed superannuation funds

Our Interest

Trisuper Auditors provides SMSF auditing services to clients of small to medium accounting practices predominately located in regional NSW and QLD. The typical firm we work with would resemble a two-partner firm with around 50 SMSF clients.

Current position of the SMSF Audit Industry

The past ten years has seen significant changes in the relationship of the SMSF Trustee, the advisor/accountant and the SMSF auditor.

In the last ten years the ATO, ASIC and the professional bodies have required SMSF audits to be undertaken by an independent auditor. In fact the ATO states "SMSF auditors have a critical role in helping to maintain the health and integrity of the SMSF sector through the annual audit of each SMSF.

Practically this have forced small to medium firms to engage a non-related external SMSF auditor.

As a result of a lot of work and education, the SMSF auditor and Accountant have developed a close working relationship in conjunction with the SMSF Trustee. The Accountant has retained the main relationship with the Trustees, however the SMSF auditor plays a critical role as the technical advisor and the "bad cop" to ensure the Trustee stay within the lines.

Our experience indicates that Trustee behaviour and consequently compliance with the SIS and SISR have improved dramatically over the past decade.

The tripartite relationship of the auditor, accountant and Trustee is starting to pay dividends in terms of timely lodgements and compliance. We are on the right track.

Since July 2013, SMSF audits have also been required to register with ASIC as a registered SMSF auditor. This has resulted in the number of SMSF auditors decreasing by 50% as per the below ATO statistics. In addition, they are required to abide by the independence and the education and

Leaders in the Trilateral Approach to Super Fund Auditing

T: 1300 874 787 A: PO Box 2125 Dangar NSW 2309 W: trisuperauditors.com.au

Liability limited by a scheme approved under professional standards legislation

experience regulations. The qualification and education requirements of the SMSF auditor have never been more burdensome.

<https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Super-statistics/SMSF/Self-managed-superannuation-funds--A-statistical-overview-2015-2016/?anchor=Appendix1Datatables#Appendix1Datatables>

<https://www.ato.gov.au/Super/Self-managed-super-funds/SMSF-auditors/>

<https://www.ato.gov.au/Forms/SMSF-independent-auditor-s-report/>

Budget Measure Proposal

The Government has proposed a budget measure in the 2018-19 Budget to change the annual audit requirement to a three-yearly requirement from 1 July 2019 for SMSFs with a history of good record-keeping and compliance. The objective of the measure is to incentivise good record-keeping and compliance by SMSFs whilst maintaining system oversight and integrity.

Under this measure, audits conducted for SMSFs on a three-yearly audit cycle will cover all of the three preceding years, maintaining integrity within the SMSF sector. SMSFs that do not meet the eligibility criteria will not be eligible for a three-yearly audit cycle and will continue to be annually audited.

The Budget proposal aims to allow SMSFs with a history of good record keeping the choice to move to a three-yearly audit cycle which will result in the following benefits for SMSF trustees, including:

- a reduction in the compliance burden on SMSF trustees while maintaining appropriate visibility of errors in financial statements and regulatory breaches;
- a potential reduction in administrative costs and auditor fees for SMSF trustees due to less frequent audits. Annual fees for SMSF auditors range from less than \$500 to over \$2,000. For 2016, the average auditor fee was \$694 and the median was \$550; and
- an incentive for SMSF trustees to submit SARs in a timelier manner.

Treasury has now released a follow up discussion paper <https://treasury.gov.au/consultation/c2018-t304424/> and is seeking feedback on the proposed budget measure.

TriSuper Auditors' Synopsis of the Proposed Measure – If it ain't broke..

After consulting with our accounting practice partners, fellow SMSF auditors and our own considerations, we are of the view this proposed measure should not proceed. There should be no change to the current regulations requiring every SMSF undergo a yearly audit.

We contend the measure if implemented would:

- increase the compliance burden on SMSF Trustees and increase errors in financial statements and increase the number of regulatory breaches.
- Increase administrative costs and audit fees.
- Destabilise the established tripartite Accountant, Auditor, Trustee relationship

- Encourage illegal early release schemes
- Place member accounts at increased risk of maladministration.

Discussion

To say that this measure came as a surprise is an understatement. It was a true budget bolter, a thought bubble formed without any understanding or apparent consultation with the SMSF industry.

Not surprisingly, Treasury has been forced to backtrack and now undergo an industry consultation process.

We have been involved in this process sitting in on recent Treasury face to face consultations with key stakeholders.

What do we think the three-year audit cycle will bring?

1. Increased compliance burden on SMSF Trustees and increased errors in financial statements and increased number of regulatory breaches.

This budget measure will undoubtedly place greater burden on the Trustees and their accountants in terms of self-determining the ability to use the three-year cycle. They will now be required to self-assess, presumably based on their compliance with certain provisions with the SIS Act and prior lodgement history. No doubt the Trustees will rely on their accountant to provide this advice.

Will the ATO be providing additional education to Trustees to help them self-assess? Will the ATO and ASIC be comfortable with the accountant providing advice as to SIS compliance? Does this fly in the face of the current independence requirements of auditors?

Treasury seems to have missed the importance the auditor management letter plays in ensuring SMSF's remain compliant. Our records show that 25% of issued management letters provide advice to the Trustees that the Fund has either breached a section of the SIS Act or is in danger of doing so if they do not take corrective action. In 90% of cases the Trustees take our advice resulting in clean audits the following year. We fear that under a three-year cycle, these minor issues will be missed in years 1 and 2 resulting in material breaches by the time year three rolls around.

Problems that accrue over three years are costly and timely to fix when they could have been nipped in the bud in year 1.

2. Increased administrative costs and audit fees

Treasury notes that one of the aims of the proposal is to reduce administrative and compliance costs for Trustees of SMSF's. We are not sure where this cost saving will occur. The audit fee is one of the lowest costs of running a SMSF. The cost of adviser and accountants' fees are by far the greatest cost burden which will continue to be incurred every year.

The SMSF will still need to have financial statements and income tax returns prepared each year and will still need to deal with other compliance matters such as minutes of meetings, reviews of investment strategies and dealing with member issues. The Trustee and accountant will still also need to review the Fund to ensure it will meet the requirements for the three-year cycle which may still involve talking to the auditor.

In addition, the auditor will still be required to conduct an audit for each year in the three-year cycle. As a result, the work and time and resulting audit fee will not materially drop. We also believe that costs may increase as a result of the auditor finding problems with year 1 or 2 which will then require the accountant to go back and amend prior years resulting in further increased costs.

3. Destabilise the established tripartite Accountant, Auditor, Trustee relationship

Looking back ten years, it was common for the accountant who prepared the SMSF financial statements to also audit the Fund. This of course resulted in conflict of interests and brought about the accounting bodies, the ATO and ASIC introducing independence requirements. ASIC also introduced the SMSF auditor registration regime.

The SMSF auditing industry has invested considerable time and resources to educate accountants and trustees the benefits of outsourcing the audit function. We have come along way with the assistance of ASIC and the ATO resulting in the majority of SMSFs appointing an auditor independent of the account. In the main, trustees and accountants understand and have become comfortable with this process. It is working well after much effort.

The proposed budget measure will undoubtedly weaken this relationship and will place the accountant back in the position of advising the Trustees on SIS compliance in years 1 and 2 of the cycle. This is dangerous territory. Accountants will undoubtedly be put in positions of conflict.

What will be the ATO and ASIC position on this?

4. Encourage illegal early release schemes

“Whilst the cats away...”

Unfortunately, it is human nature for greater instances of non-compliance to occur when the police are not on the beat. We believe a three-year audit cycle will provide cover for greater illegal behaviour by trustees and scheme promoters.

Circumstances in the personal and business life of trustees can rapidly change. A fund that was perfectly compliant can quickly change. We have seen many examples of a trustee facing a personal or business crisis who all of a sudden borrows large amounts of monies from a SMSF bank account. Under the current arrangement this will likely be picked up within 12 – 18 months. Under the proposed measure, this could blow out to 36 plus months. To us, this is unacceptable.

No doubt, some trustees will take advantage of this increased timeframe to being audited and no doubt unscrupulous advisors and promoters will circle.

Why implement this proposed measure when it will result in increased illegal activity?

5. Place member accounts at increased risk of maladministration

In a Utopian world, all Trustees of a SMSF would have equal knowledge, ability and power in the Fund's management and reporting. In the real world nothing could be further from the truth.

The majority of SMSFs are family based and it is common for one Trustee to be the dominant decision maker and it is not unusual for the other trustees to have little to do with the operation of the Fund. That is the reality.

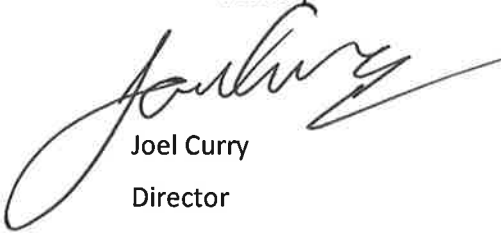
How then are the interests of all the members monitored, measured and reported on? The current arrangement of annual audits goes some way to protecting the interest of members who may otherwise not have the power to obtain information on their super interests.

We fear a three-year cycle will disadvantage the ability of these members to obtain timely information and may open up risk of fraud and maladministration by the dominate Trustee.

Why implement this proposed measure and risk members interests?

We thank-you for the opportunity to provide a submission to this proposed measure and welcome you to contact us for any further discussion you may feel appropriate.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Joel Curry', with a long, sweeping underline that extends to the right.

Joel Curry

Director