

# Association of ARP Unitholders Incorporated

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Future of Financial Advice  
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## Submission to the Future of Financial Advice Options Paper

This submission is made by the Association of ARP Growth Fund Unitholders Inc (the Association).

The objectives of the Association are:

*" To represent and promote the interests of investors in entities managed by or otherwise associated with ( or formerly managed by or associated with ) Trio Capital Limited ( including the ARP Growth Fund ), to lobby relevant authorities in respect thereto, to seek compensation for members in respect thereto, to provide information to members in respect thereto and to undertake activities incidental thereto. "*

1. **Self Managed Superannuation Funds (SMSF's) need improved levels of regulatory protection.**
  - a. The Association wishes to make a specific point in relation to the discussion on the distinction between retail and wholesale clients in regard to those clients considered to be in need of regulatory protection.
  - b. Following the *Wallis Inquiry* in 1997, the *Corporations Act* was amended by the *Financial Services Reform Act 2001* to establish a difference between the levels of consumer regulatory protection offered to retail and wholesale clients.
  - c. Generally retail clients enjoy a higher level of consumer protection as they are deemed to be less well informed and therefore less well able to assess the risks involved in financial transactions.
  - d. The one notable retail exception to this general principle appears to lie in the field of Self Managed Superannuation Funds (SMSF's), in particular in regard to the total exclusion of SMSF's from the consumer protection offered to the members of other regulated superannuation funds under part 23 of the *Superannuation Industry (Supervision) Act (SIS)*.
  - e. The Association questions the appropriateness of this broad exclusion and in particular the apparent total extent of its applicability. The Association believes it should be modified to better cater for situations in which SMSF retail members are clearly disadvantaged under circumstances in which *regulated* retail (and wholesale) superannuation funds may qualify for consumer protection under part 23 of *SIS*, yet SMSF retail clients in a precisely similar position are excluded from this protection.
  - f. This is, in the view of the Association, an unintended anomaly which should be addressed as one of the outcomes of the Future of Financial Advice review process. By so doing, the Association believes that the Federal Government will be able to better provide regulatory

protection to this significant and growing group of retail SMSF investors, in those specific circumstances where such additional protection is clearly warranted.

- g. The absence of such protection appears not only to be confusing to such clients, but also to many providers of financial advice upon whose advice these clients initially base their superannuation decisions. The trustees of SMSF's are currently treated more like "professional investors", akin to the mostly professional trustees of large regulated superannuation funds, whereas they should in fact generally be regarded as less sophisticated retail clients. Indeed, many of them are retail small business owners.
- h. The Federal Government is seeking to draw a line as to which investors need improved protection. The Association believes that the great majority of SMSF's clearly fall into the retail category and should be entitled to the greater levels of regulatory protection enjoyed by such clients, in specified situations of fraudulent conduct or theft.

## 2. What needs to be altered to improve levels of regulatory protection for SMSF's?

- a. Currently only the trustee of an APRA regulated superannuation fund can apply to the Minister for a grant of financial assistance, if the fund suffers an "eligible loss" as the result of fraudulent conduct or theft. The same legislation specifically excludes the trustees of SMSF's, regulated by the Australian Tax Office, from applying for similar assistance, even under circumstances which are identical.
- b. The Association believes that this outcome was never the intended outcome of the 2003 *Review into Part 23 of the SIS Act (1993)*. The general philosophy underpinning the prudential regulation of superannuation is that the trustee of a superannuation fund bears primary responsibility for the fund's prudent operation. Nevertheless, recognising the importance of financial stability, the Government also applies an additional layer of prudential regulation to promote sound risk management. Furthermore, it is recognised in the *SIS Act* that in the case of fraud or theft that there is a case for Government intervention to provide compensation, in particular under part 23.
- c. The exclusion of SMSF's from the part 23 protection was originally justified on the grounds that the SMSF trustees are also fund members. It was therefore assumed that the trustee(s) will act in their own best interest and that as a result "members do not need the full range of statutory measures to protect them in relation to the conduct of the trustee" (*Review page 4*).
- d. While there may be some logic to this approach, it also carries clear limitations. The Association is of the view that this exclusion operates unduly harshly against the members of SMSF's under certain circumstances and needs to be amended to provide them with greater regulatory protection.
- e. The circumstances in which improved protection is required are those in which SMSF trustees act in good faith and to the same standards as those trustees of regulated superannuation funds, and yet their members are grossly disadvantaged in cases of fraudulent behaviour and/or theft. The fact that, under the same set of circumstances, the members of the regulated funds are eligible to apply for compensation, whereas the members of a SMSF are not, is clearly one capable of causing gross inequity.
- f. The anomalous treatment of SMSF's is well illustrated in the current case of the liquidation of the superannuation funds managed by *Trio Capital*, including the *ARP Growth Fund*. These Funds were wound up in the Courts in 2010, Justice Palmer being moved to remark that the events which led to this liquidation amounted to a "scandalous fraud". The Trio Capital funds included both regulated superannuation funds and SMSF's.
- g. The trustees of both types of funds made their investment decisions based upon information provided from the same documentation, using identical product disclosure statements issued under the guidelines of, and with the approval of, the appropriate Australian Government Regulator. (It has indeed even been suggested in the media that the product disclosure

statements themselves were deficient in terms of the use to which investor money was to be put.)

- h. Both sets of trustees clearly formed the view that, based upon the information provided in those Regulator approved documents, it was in their members' interest to invest in the Trio Capital managed products. Yet when it turned out that they had all been subject to the same complicated deception and fraud, only the members of one group had an avenue of appeal open to them under part 23, namely those under regulated funds.
- i. In a post GFC environment in which improved investor protection is a stated Government priority, it is no longer possible to justify the discriminatory treatment suffered by members of SMSF's such as outlined in the case above. The Minister for Financial Services and Superannuation, in his response to the Cooper Review, has promised to provide superannuation members with improved levels of protection and this is clearly a case where such improved protection is required.

### 3. Recommendation

The Association believes that public policy dictates that an improved level of protection for SMSF members is warranted under the extreme conditions outlined above. The Association therefore recommends that the Federal Government move to include the ability for SMSF members, who act in good faith and who are nevertheless the innocent victims of fraudulent behaviour or theft by external third parties, to be able to apply to access the provisions of part 23 of the *SIS Act*.

Please do not hesitate to contact the undersigned should you require any further information.

Yours sincerely,



**Ron Thornton**  
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