



## FACT SHEET

### PRODUCT DISCLOSURE STATEMENTS AND SELF-MANAGED SUPERANNUATION FUNDS

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#### 1. History of PDS's and SMSF's

Since 11 March 2004, when the final provisions of the *Financial Services Reform Act 2001* came into effect, there has been much confusing information regarding the need for SMSF's to develop and maintain Product Disclosure Statements (PDS's).

#### 2. The Original Situation

When the *Financial Services Reform Act 2001* was first released, it contained a provision which would have required all SMSF's admitting new members to prepare PDS's and to lodge PDS in-use notices with the ASIC. As you are no doubt aware, PDS's require information such as the name and address of the trustee, the basic structure of fund benefits, fees to be charged, and so on.

#### 3. How the June 2003 Exemption for SMSF's Arose

It was pointed out to the Government that, given the requirement that all members of a SMSF must be trustees or directors of a corporate trustee, requiring SMSF's to prepare PDS's would be equivalent to the trustees telling themselves where they lived, what they intended to do and so on. Worse still, there was no way that ASIC was geared up to accept between 20,000 and 30,000 PDS in-use notices from new SMSF's each year.

Finally, in the middle of last year, common sense prevailed. However, in the highly charged atmosphere of "one regulatory scheme for all" and "no exemptions to be given" which surrounded FSR, it was decided that a straight-out exemption for SMSF's would

seem like a back-down. So, they produced a "Clayton's" exemption (you remember Clayton's? "The drink you're having, when you're not having a drink."). At the outset this exemption was interpreted to exempt SMSF's from the PDS provisions in all cases, except where a trustee had been either virtually coerced, or so disinterested as to have breached their duty as trustee.

#### 4. The SMSF Exemption From PDS Requirements

Let's look at the legislation. Section 1012D(2A) states (emphasis added):-

"In a recommendation situation or issue situation, the regulated person *[the trustee]* does not have to give the client *[the member]* a Product Disclosure Statement for the financial product if:

- (a) the financial product is an interest in a self-managed superannuation fund; and
- (b) the regulated person *[the trustee]* believes on reasonable grounds that the client *[the member]* has received, or has, and knows that they have, access to, all of the information that the Product Disclosure Statement would be required to contain."

#### 5. What Does the Exemption Section Mean?

What does this mean? Let's look at the Explanatory Memorandum to the *Financial Services Reform Amendment Bill 2003*, which introduced this change. Addressing this issue, it stated (emphasis added):-

"The proposed exemption provides that the obligation to give a PDS does not apply in circumstances where prospective members have the information available to take an informed decision. For example, a PDS would not be required to be provided in circumstances where all the prospective members/trustees of a fund have, or have available to them, the relevant information or where the fund has only one member."

In other words, a one member fund cannot ever be required to produce a PDS, as the member is presumed to run the fund and know everything that is going on. Some promoters have argued that, unless a potential member has significant knowledge about the operation of SMSF's, an advisor cannot presume that they have access to the PDS information. The EM clearly shows that this was *not* the Parliamentary intention at all. If that were the case, they would have envisaged many cases where a single member fund would need a PDS.

#### 6. How Will ASIC Police Compliance by SMSF's?

Saying that a PDS must be provided if the member does not have access to the information which a PDS would otherwise contain is all very well in theory, but how is ASIC ever to prove that one member doesn't know what is going on in the fund? In speeches and other publications regarding the policing of disclosure, ASIC have admitted that they will only investigate SMSF's where they receive a specific complaint.

#### 7. How are Promoters Linking Liability to Accountants and Financial Planners?

The argument to date is that an aggrieved member will make a formal complaint that they did not know what was happening, which in turn would lead to civil and perhaps criminal prosecution against their co-trustee/s, then the person who assisted them in establishing

the fund would be implicated under the *Crimes Act (Clth) 1914* as having "aided and abetted" in the commission of a crime (i.e. their accountant, financial planner, etc.). We believe that the possibility of such a line of reasoning being successful is remote. Bear in mind that, even before they attempt to convince the Court that their advisor was an accomplice in their own lack of access, they must prove that they did, in fact, lack the requisite access.

#### 8. Admitting to Needing a PDS May Amount to an Admission of Negligence

Regardless of the likelihood of an action succeeding, we question whether any member/trustee will ever admit to lacking access to the requisite information. Consider the following points (which are far from a complete list):-

- From Section 52(2), here are two of the compulsory covenants which a trustee of a superannuation fund enters into upon signing the trust deed:-

"(b) to exercise, in relation to all matters affecting the entity, the same degree of care, skill and diligence as an ordinary prudent person would exercise in dealing with property of another for whom the person felt morally bound to provide;

(c) to ensure that the trustee's duties and powers are performed and exercised in the best interests of the beneficiaries;"

So, admission by a member that they needed a PDS amounts to an admission by the trustee of a breach of Section 52(2).

- The seminal case on the duties of new trustees is *Hallows v. Lloyd* (1888) Ch. D. 686, per Kekewich J.:-

"This raises the important question, what are the duties of persons becoming new trustees of a settlement?...I think that when persons are asked to become new trustees, they are bound to enquire of what the property consists that is proposed to be handed over to them, and what are the trusts. They ought also to look into the trust documents and papers to ascertain what notices appear among them of encumbrances and other matters affecting the trust."

So, admission by a member that a PDS should have been prepared also amounts to a breach of one of the trustee's first and fundamental duties in the law of equity.

- What is the regulator of SMSF's (the Australian Taxation Office) attitude towards trustees of SMSF's who disclaim knowledge of, or responsibility for their fund? This, from the ATO publication, "Self managed Superannuation Funds (SMSF's) – duties of trustees":-

"Trustees of self managed superannuation funds (SMSFs) are ultimately responsible for the running of their fund. It is imperative that each trustee understands the duties, responsibilities and obligations of being a trustee....If a trustee fails to act in accordance with the rules and obligations imposed on them, the trustee may be sued by affected fund members and/or may jeopardise a fund's eligibility for tax concessions. In addition, SISA imposes substantial penalties on trustees who have failed to carry out their duties."

In order for a member to bring a successful action on the basis that they should have received a PDS, one of the issues which they must argue is that they were not only unaware of what they were getting themselves into, but also that they were so disinterested in what they were signing, they did not even ask about "access" to information regarding benefits, risks, etc. We believe that such an admission would immediately draw the attention of the ATO.

#### 9. When Does a PDS Need to be Given?

We have seen a small number of organisations telling advisors that they must prepare a PDS for all SMSF's which they currently have in existence. This is *not* true. There are only two circumstances in which a SMSF might ever be required to produce a PDS:-

- When a new member joins the fund; and
- When a member changes from growth to pension phase.

A PDS only needs to be given at the stage of joining the fund to a member who won't have full access to information, or to an existing member commencing a pension when they don't have access to information about that pension. There is no obligation on, nor any need for, the trustees to keep a PDS up to date in the meantime.

#### 10. Does a PDS Need to be Given to a Member Starting a Pension?

As with all PDS's for SMSF cases, if a Member has sufficient access to the information otherwise required to be provided in the PDS, they do not need a PDS prior to commencing a pension. We suggest it would be highly unusual for an advisor to establish, say, an allocated pension for a client in a SMSF without explaining the reasons why such a pension is beneficial and the various attributes of such pensions.

Regardless of this fact, there is another issue surrounding PDS's and the move from growth to pension phase. Section 761E of the *Corporations Act 2001* sets out the circumstances in which a person is deemed to have "issued" a financial product. Where a person issues a financial product, they are required to issue a PDS (subject to the SMSF and other exemptions). Regulation 7.1.04E of the *Corporations Regulations 2001* clarifies the "issue" issue in relation to pensions. It states as follows (emphasis added):-

- "(1) This regulation applies if a member of a superannuation fund, who has a superannuation interest in the growth phase, **elects** to receive a pension in relation to that interest or part of that interest.
  
- (2) For paragraph 761E (7) (a) of the Act, the superannuation fund is taken to issue a new financial product when:
  - (a) it acknowledges receipt of the member's election; or
  - (b) it makes the first payment of the pension;whichever occurs first."

Under our trust deed, a member is automatically entitled to receive a pension when they retire. In fact, they must "elect" to receive a lump sum, should they wish to receive one. While it may still be argued that the member makes a form of election (e.g. electing to take an allocated, rather than a complying pension), our point is that there is a potential defense open to trustees who do not provide a PDS in these circumstances.

(NB. Due to the narrow scope of Regulation 7.1.29A, which exempts accountants from the licensing regime in relation to SMSF's, it is not clear how much advice unlicensed accountants can give in relation to the establishment of pensions. This is a separate issue from the obligation to issue PDS's. All of the major accounting bodies have issued detailed guides regarding the limits of unlicensed accountants' advice under Regulation 7.1.29A.)

**11. Is a "Standard" PDS Enough For a Fund Which Has Been Running for Some Time?**

Assuming that the accountant or advisor decides that they will provide a PDS to a SMSF upon the admission of a new member, or where an existing member commences a pension, the standard PDS produced for a new superannuation fund will not be sufficient. A fund which has been in existence for some time will have an investment strategy, existing investments with a return history and experience with levels of administrative expenditure.

For an existing fund, the fund's investment strategy, as well as the most recent set of financial statements for the fund should be attached as annexures to the standard PDS. The PDS should refer to the fact that these documents are attached. If these documents are not attached (e.g. by stapling them to the PDS), under Section 1013L of the *Corporations Act 2001*, they might be considered to be separate documents. Where a PDS is provided in more than one document, each document must clearly be labeled as being a PDS document and must list any other documents which are also PDS documents.

**12. Should You Provide a PDS to All New SMSF Clients?**

In our opinion, when Parliament passed Section 1012D(2A), they believed that they had exempted the vast majority of SMSF's from the requirement to produce PDS's. Until the last couple of months, this was also the opinion of the majority of industry participants.

In the last couple of months, a body of opinion has developed that accountants and advisors should always provide PDS's in these circumstances "just to be on the safe side". As noted above, we believe that the chances of any action being taken (let alone succeeding) against an advisor for one of their SMSF's failing to provide a PDS, is extremely remote.

Nevertheless, we have prepared and made available to all of our clients, at no charge, a PDS (see attached) which may be used for all SMSF's using our current trust deed.

**It should be noted that, while this PDS accurately describes the benefits and options available to members under the current deed, we make no guarantee that it would be appropriate for deeds which are more than 12 months old. Also, there is no certainty that it would be appropriate for SMSF's established using deeds other than our own.**

*Should you have any queries regarding this fact sheet, please do not hesitate to contact us on Freecall 1-800-773-477.*

## PRODUCT DISCLOSURE STATEMENT

**Name of Superannuation Fund:**

**Date of Notice:**

**Name of Member:**

**Address of Member**

This Product Disclosure Statement (PDS) may be required by Part 7.9 of the *Corporations Act 2001*, as amended, to be given to members of superannuation funds being issued with an interest in the above superannuation fund (the "Fund") for the first time. An interest in this Fund includes the acceptance of your initial application for membership and may also include your change from an accumulation or growth phase, to pension phase.

This PDS applies in respect of the Fund, so long as it remains a self-managed superannuation fund (SMSF), pursuant to the *Superannuation Industry (Supervision) Act 1993*, as amended.

Much of the information required to be provided in a PDS for a SMSF will fall into one of the following categories:-

- Information of which you are already aware (e.g. your address and contact details for the above SMSF).
- Information which your duties and responsibilities as a trustee of the above SMSF require that you be aware of, prior becoming a trustee (e.g. the terms of the trust deed and governing rules of the above SMSF).
- Where the Fund is a newly established superannuation fund, information which has not come into existence at the date of this PDS being issued (e.g. fees and charges, investment strategy and returns, etc.)

It is important to note that this information relates to your membership of the Fund, not to your obligations as a trustee of the Fund. It is up to you to decide whether or not you wish to take on the responsibility of trusteeship of a SMSF, however you cannot be a member of a SMSF without also being a trustee or director of a corporate trustee of the Fund. You should separately familiarise yourself with your trustee duties.

Pursuant to Section 1013D of the *Corporations Act 2001*, as amended, the following information is provided to you:-

### **Name and Contact Details of the Product Issuer**

The above SMSF is the issuer of this PDS. The Fund's contact details are determined by you and (where applicable) your co-trustee(s) (or director(s) of a corporate trustee). They will either be your own address, or an address to which you have previously agreed and been made aware of.

### **Benefits**

The benefits available to you are set out in the above SMSF's trust deed. As a member of a SMSF, with the agreement of your co-trustee(s), you can choose any form or combination of retirement benefits legally available – you have as much flexibility as is possible.

Your primary form of retirement benefit is a "pension", as that term is defined in the *Superannuation Industry (Supervision) Regulations 1994*, however you may choose a lump sum benefit, by request made in writing at the time you wish to take your benefits. Other benefits potentially available to

you include: death benefits, total and permanent disablement benefits and total and temporary disablement benefits.

Once you have "retired" after age 55 years, you will be entitled to commence to take your superannuation benefits. Any decision (except for the option to take a lump sum) may be verbal, but should preferably be in writing. It should be noted that the timing and types of superannuation benefits you may be entitled to take is the subject of regular legislative change. As such, you should check what options are available to you, at the time you are ready to start taking your benefits.

There may be significant taxation and other implications, should you choose to take your retirement benefits in one form or another. The area of benefits design is a complex, but critical area to ensuring the value of your superannuation savings are maximised. As such, we strongly recommend that you seek professional advice, prior to taking any benefits.

### **Nominating Beneficiaries**

You may make different types of nominations in relation to the payment of your benefits upon your death. The first is contained in your Application for Membership of the Fund. This nomination is not binding on the trustee and may be open to challenge by any potential beneficiaries. Nevertheless, the trustee must give this nomination serious consideration and would require good reasons not to distribute in accordance with these wishes.

The other types of nominations are called a Binding Death Nomination or Non Lapsing Binding Nomination. This nomination must meet certain forms, including being signed by two independent witnesses (for Binding Death Nominations) and at least once every three years being confirmed, modified or repealed by notice in writing from you to the trustee. The requirements to be followed in relation to Binding Death Nominations or Non Lapsing Binding Nominations are to be found in the trust deed. You should be aware that the trustee cannot deviate from the terms of a valid, binding nomination, even if the consequences of complying with it would result in higher tax than might be possible via other avenues, or where you have changed your mind about the beneficiaries or the amounts they should receive. As such, it is important that you seek professional advice prior to submitting a Binding Death Nomination or Non Lapsing Binding Nomination.

### **Risks**

This SMSF is an accumulation fund. This means that amounts (including contributions, transfers and rollovers and accumulated earnings) are invested as you and your co-trustees (or director(s) of a corporate trustee) see fit.

Depending upon the investment decisions which you as trustee and any of your co-trustees/co-directors make over time, you will either accumulate investment gains (including capital and income gains) or accumulate investment losses. In some years, gains may arise and in other years, losses may arise. This will affect the balance of your member's accumulation account. As a trustee, you have both the responsibility for and control over the manner in which the Fund's investments are made and, as such, you control the risks associated with the Fund's investments.

### **Amounts Payable and Fund Expenses**

As a trustee of the SMSF, you and your co-trustee(s)/co-director(s) control any amounts which might be payable for the issue of your membership in the Fund. Costs and expenses of the Fund may either be shared equitably among members by way of deduction from their accounts or, where the expense relates to identifiable members only, from those members' accounts.

### **Commissions**

As a trustee of the SMSF, you and your co-trustee(s)/co-director(s) control any appointments of financial professionals and investments into products which might include commissions.

### **Dispute Resolution**

The dispute resolutions mechanisms available to members are found in the Fund's trust deed. As a trustee, it is reasonable to presume that you have familiarised yourself with the contents of the trust deed. As such, pursuant to Section 1013F of the *Corporations Act 2001*, as amended, detailed information concerning the dispute resolution mechanisms available under the deed are not included in this PDS.

### **Taxation Implications**

All superannuation funds in the accumulation phase pay 15% tax on their net taxable incomes. Net taxable income includes assessable contributions, plus investment earnings, less deductible expenses. Other rebates and credits, such as franking rebates and imputations credits may reduce the amount of tax which a superannuation fund must pay. Net taxable capital gains of a superannuation fund are taxed at 10%.

Each year, the trustee will make a determination as to how these taxes are to be deducted from an individual member's account. The trustee is required to determine this in an equitable manner, as between the members.

Depending on your personal taxable income in a given year, there may also be a liability for the superannuation contribution surcharge tax in respect of any tax-deductible contributions made by your employer or yourself. Where surcharge is payable, this amount will be directly deducted from your member's account.

The income and capital gains of a superannuation fund which is paying one or more pensions will be exempt from tax, to the extent that the assets of the Fund are considered to be supporting those pensions (and taxable to the extent that those assets are considered to be supporting continuing accumulations and reserves). The amount of tax which you as trustee and your co-trustee(s)/co-director(s) consider to be a reasonable and equitable allocation for each member each year will be deducted from the balance of your member's accumulation account.

The rules regarding personal taxation of superannuation benefits are far too complex to address in this document. It is strongly advised that you seek professional advice regarding the taxation of your personal superannuation benefits and the options available to you.

### **Cooling-off Period**

There is a fourteen (14) day cooling-off period from the date you are issued with membership of the above SMSF, during which time you may cancel your membership of the Fund. Note that the trustee must receive notification of your membership cancellation prior to the expiry of this period, in order for it to be considered effective. Note also that the cooling off period relates to your membership only and does not give you a right to resile from your duties as a trustee of the Fund (including payment for the establishment of the Fund itself).

### **Insurance**

There is no obligation for the trustee of the Fund to take out life or other insurances on your behalf. Obviously, however, as a trustee of the Fund, you are in a position to make such application. As noted above, benefits can be paid out in similar circumstances to normal insurable events (death, total and permanent disablement, total and temporary disablement), however where the Fund has not undertaken insurance on your behalf, any payments will be limited to the value of your member's accumulation account.

### **Alternative Types of Superannuation Funds**

You should be aware that there are a number of alternative forms of superannuation available to you, each of which have different characteristics. You should consider your own situation carefully

prior to becoming a member of one form of superannuation fund or another, and should seriously consider seeking advice from an authorised representative of an Australian financial services licensee.

#### Public Offer Superannuation Funds

These funds are managed by a trustee on your behalf. You may have a choice of broad "categories" for investment, such as conservative, balanced, growth, etc., where you have no control over the actual investments which are undertaken by the fund (and, depending upon their reporting, you may never know what those assets are). Certain other funds allow members (usually only through a financial planner) to select individual investments from a menu of options. An example might be a list of 50 managed funds and shares in the top 200 ASX listed companies. Typically, you will only receive written reports on your share of the fund's performance annually in your member statement, although you may be able to access interim performance results for the fund (e.g. via a website). Fees will usually be charged on entry and exit from these funds. There will also be contribution fees, administration fees, category switching fees (often only after a certain number of free annual switches) and asset management fees. Some of these fees would normally be charged as a percentage of your account balance. Many public offer funds will include a commission payable to the advisor who recommends the fund to you. In most cases, the more investment choices you have, the higher the overall level of fees the fund charges. Typically, you can also purchase insurance (life, total and permanent disablement and sometimes total and temporary disablement). Furthermore, public offer funds may restrict the types of benefits which are payable upon your death or retirement (e.g. they may not pay certain types of pensions, or may require you to transfer to another sub-category within their fund before paying pensions).

#### Industry Superannuation Funds

These funds are managed by a trustee on your behalf. In the past, these funds have only been open to members of a certain union or industry, however many are now accepting membership from other parties. You may not have a choice of "categories" for investment in these funds, although many now offer similar choices of categories to public offer funds, such as conservative, balanced, growth, etc. Once again, you have no control over the actual investments which are undertaken by the fund (and, depending upon their reporting, you may never know what those assets are). Typically, you will only receive reports on your share of the fund's performance annually in your member statement, although you may be able to access interim performance results for the fund (e.g. via a website). Where categories are available, there will normally be restrictions on the frequency with which you can change between categories. Fees will usually be charged on entry and exit from these funds. There may also be contribution fees, administration fees, category switching fees (often only after a certain number of free annual switches) and asset management fees. Some of these fees will normally be charged as a percentage of your account balance. Industry funds do not normally pay commissions to advisors who recommend the fund to you. Typically, a certain level of "group" insurance (life, total and permanent disablement and sometimes total and temporary disablement) will be provided by industry funds without medical requirements. Additional insurance can be acquired with medical examination. Industry funds may restrict the types of benefits which are payable upon your death or retirement (e.g. they may not pay certain types of pensions, or may require you to transfer to another sub-category within their fund before paying pensions).

#### Small APRA Funds

These funds are similar to SMSF's, except that they have an independent trustee. The independent trustee must be an "approved" trustee. Typically, these are large public trustee corporations. They will charge fees for their services and all decisions as to investments, benefit payments and the like must be approved by them. They will normally control the fund's cheque book and appoint the accountants and auditors of the fund. They are normally only chosen when a member wishes to have investment flexibility close to that of a SMSF, but for one reason or another, they cannot be a trustee of their own fund (e.g. because they are an undischarged

bankrupt and therefore a “disqualified” person, or because the trustees are leaving Australia for more than two years, which can have adverse tax consequences). Because of the expense of the approved trustee services, these funds are only used in a very limited number of cases.

There are two other types of superannuation fund - employer-sponsored superannuation funds and public sector superannuation schemes - which are not discussed here, as they are not a type of fund which a member can typically “choose” to join (your employer will make the choice to contribute to such a fund, without reference to you as an employee).

**Other Information**

The first duty of a trustee is to familiarise themselves with the terms of and their duties under the trust. Pursuant to Section 17A of the *Superannuation Industry (Supervision) Act 1993*, as amended, all members of SMSF’s must be trustees (or directors of the Fund’s corporate trustee).

This PDS addresses issues relating to your proposed membership of the Fund, not issues which arise in relation to your duties and liabilities as a trustee of the Fund. As a trustee, it is your responsibility to separately familiarise yourself with those duties and liabilities and to be actively involved in the operation of the Fund. As this is a legal obligation, it is reasonable to presume that you have done so. As such, pursuant to Section 1013F of the *Corporations Act 2001*, as amended, detailed information concerning other matters pertaining to the operation of the Fund are not included in this PDS.

**Other Documents Forming Part of This PDS, For Funds Other Than New Funds**

Where the Fund is a pre-existing fund and you are joining as a member, or where you are an existing member and are commencing to take your benefit in the form of a pension, you will find the following documents annexed to this PDS:-

- The Fund’s investment strategy; and
- The last financial statements prepared in respect of the Fund.

These documents form part of this PDS for funds other than newly established funds. If you have not yet received a copy of these documents, you should not sign this PDS until you have received them.

<p><b>I have read and understood this Product Disclosure Statement, prior to signing my Application for Membership:-</b></p> <p><b>Signature:</b> .....</p> <p><b>Print Name:</b> .....</p> <p><b>Date:</b> ...../...../.....</p>
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