

## **EXPLANATORY STATEMENT**

### **Select Legislative Instrument 2012 No. 183**

#### **Issued by authority of the Minister for Financial Services and Superannuation**

##### *Superannuation Industry (Supervision) Act 1993*

##### *Superannuation Industry (Supervision) Amendment Regulation 2012 (No. 2)*

Subsection 353(1) of the *Superannuation Industry (Supervision) Act 1993* (the SIS Act) provides, in part, that the Governor-General may make regulations prescribing matters required or permitted by the SIS Act to be prescribed, or necessary or convenient to be prescribed, for carrying out or giving effect to the SIS Act.

Subsection 31(1) of the SIS Act provides that the regulations may prescribe standards applicable to the operation of regulated superannuation funds and to trustees of those funds.

Subsection 35B(2) of the SIS Act states that the regulations may provide for, or in relation to, the preparation of accounts and statements covered by subsection 35B(1) of the SIS Act. If the regulations do so, the accounts and statements covered by subsection 35B(1) must be prepared in accordance with the regulations.

The purpose of the Regulation is to amend the *Superannuation Industry (Supervision) Regulations 1994* (the SIS Regulations) to require:

- trustees of self managed superannuation funds (SMSFs) to consider insurance for their members as part of the fund's investment strategy;
- money and other assets of an SMSF be kept separate from those held by a trustee personally and by a standard employer-sponsor or an associate of a standard employer-sponsor (a standard employer-sponsor is an employer that contributes, or would contribute, wholly or partly pursuant to an arrangement between the employer and a trustee of the regulated superannuation fund concerned); and
- SMSF assets to be valued at market value for reporting purposes.

On 16 December 2010, the Minister for Financial Services and Superannuation, the Hon Bill Shorten MP, announced the Stronger Super reforms. Stronger Super represents the Government's response to the review into the governance, efficiency, structure and operation of Australia's superannuation system, the Super System Review. The proposed Regulation implements three key Stronger Super reforms.

The Regulation specifies that trustees are required to consider whether the fund should hold a contract of insurance that provides insurance cover for one or more members of the fund. This will ensure that members consider their personal circumstances in regards to their need for insurance cover such as life insurance.

The Regulation also specifies that a trustee of an SMSF must keep money and other assets of the fund separate from any money and assets held by the trustee personally or by a standard employer-sponsor or an associate of a standard employer-sponsor of

the fund. In making this requirement an operating standard, the Australian Taxation Office will have a direct power to enforce this requirement.

The Super System Review found that the differing valuation methods used by SMSFs has a significant impact on a member's ability to ascertain current superannuation benefits and affects the reliability and usefulness of superannuation data.

The Regulation also specifies that when preparing accounts and statements required by subsection 35B(1) of the SIS Act, including a statement of financial position and an operating statement, an asset must be valued at its market value. This ensures that all SMSFs use one valuation method which will improve the reliability and usefulness of SMSF data. This also ensures that SMSF members are given an accurate picture of the current financial position of the fund and their entitlements by not allowing SMSFs to use historical value for asset valuations.

Details of the Regulation are provided in the Attachment.

The SIS Act specifies no conditions that need to be satisfied before the power to make the Regulation may be exercised.

The Regulation is a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

The Regulation commences on the day after it is registered.

Public consultation on these measures was undertaken as part of Stronger Super. The Government established the Stronger Super Peak Consultative Group, comprising of representatives from peak industry, employer, employee and consumer groups to provide broad, high level advice on the design and implementation of the Stronger Super reforms. In addition, the Government established the SMSF working group to provide technical input on the SMSF reforms. The working papers presented and discussed at the SMSF working group meetings were published on the Stronger Super website and public submissions were invited.

Public consultation was also undertaken between 21 May and 1 June 2012 when an exposure draft of the Regulation was released. Seven submissions were received in response to this consultation, six of which were public submissions and one was confidential. The public submissions are available on the Stronger Super website.

Authority: Subsections 353(1) of the  
*Superannuation Industry  
(Supervision) Act 1993*

**Details of the *Superannuation Industry (Supervision) Amendment Regulation 2012 (No. 2)***

**Section 1 – Name of Regulation**

This section specifies the name of the Regulation as the *Superannuation Industry (Supervision) Amendment Regulation 2012 (No. 2)*.

**Section 2 – Commencement**

This section provides for the Regulation to commence on the day after it is registered.

**Section 3 – Amendment of *Superannuation Industry (Supervision) Regulations 1994***

This section provides that Schedule 1 amends the *Superannuation Industry (Supervision) Regulations 1994*.

**Schedule – Amendments**

**Item [1]**

Item [1] makes a minor amendment to accommodate a further paragraph in subregulation 4.09(2).

**Item [2]**

Item [2] inserts a new paragraph into subregulation 4.09(2) applicable to trustees of self managed superannuation funds (SMSFs). Paragraph 4.09(2)(e) is intended to ensure that trustees of SMSFs consider whether they should hold a contract of insurance that provides insurance cover for one or more members of the fund.

Regulation 4.09 requires trustees to formulate, regularly review and give effect to an investment strategy having regard to the whole circumstances of the fund. One circumstance SMSF trustees must have regard to is whether the trustees should hold insurance for their members, such as life insurance.

The Super System Review panel noted that less than 13 per cent of SMSFs have insurance and that SMSF members were more likely to hold appropriate levels of insurance, or be able to hold insurance outside their superannuation, than members of other superannuation funds. In making its recommendation, the panel wanted to ensure that trustees consider holding insurance for SMSF members.

Trustees of SMSFs are expected to be self-reliant in determining the type and level of insurance cover members might require whether within or outside their SMSF. In meeting this requirement, trustees should have regard to the personal circumstances of their members and other legislative requirements such as the sole purpose test in section 62 of the *Superannuation Industry (Supervision) Act 1993* (the SIS Act).

Trustees may evidence this requirement by documenting decisions in the fund's investment strategy or minutes of trustee meetings that are held during the income year.

Regulation 4.09 is a prescribed standard applicable to the operation of superannuation entities. Section 34 of the SIS Act provides that a person who intentionally or recklessly contravenes this standard is guilty of an offence punishable on conviction by a fine not exceeding 100 penalty units.

### **Item [3]**

Item [3] amends subregulation 4.09(2) to require trustees to regularly review the entity's investment strategy. Trustees should conduct a review of the entity's investment strategy on a regular basis to take into account factors such as the changing circumstances of their fund and its members.

Trustees may evidence this requirement by documenting decisions in the minutes of trustee meetings that are held during the income year.

### **Item [4]**

Item [4] inserts regulation 4.09A to require that a trustee of an SMSF keeps money and other assets of the fund separate from any money or assets held by the trustee personally or by a standard employer-sponsor or an associate of a standard employer-sponsor. A standard employer-sponsor is defined in subsection 16(2) of the SIS Act as an employer who contributes, or would contribute, wholly or partly pursuant to an arrangement between the employer and a trustee of the regulated superannuation fund concerned.

This requirement, applicable to all trustees of SMSFs, is currently established by way of a covenant taken to be incorporated into the governing rules of the fund. Consequences of contravening a covenant are limited to actions between the parties affected by and involved in the contravention. The Australian Taxation Office (ATO) is unable to enforce compliance with covenants and relies on voluntary compliance by trustees.

The Super System Review panel noted that breaches of the existing covenant occur with some frequency, such as where an SMSF operates using a member's personal bank account rather than through a separate account established for the SMSF, or where assets are recorded in one or more member's name personally, rather than in their capacity as trustee of the SMSF. Contraventions of the existing covenant are one of the most commonly reported contraventions reported to the ATO.

Regulation 4.09A is a prescribed standard applicable to the operation of superannuation entities. Section 34 of the SIS Act provides that a person who intentionally or recklessly contravenes this standard is guilty of an offence punishable on conviction by a fine not exceeding 100 penalty units.

### **Item [5]**

Item [5] inserts Regulation 8.02B to require that for the year of income 2012-13 and any later year of income, when preparing accounts and statements required by

subsection 35B(1) of the Act, an asset must be valued at its market value. SMSFs must begin to value their assets at market value when preparing the fund's accounts and statements for the 2012-13 year of income.

The term 'market value' takes the same meaning as provided in subsection 10(1) of the SIS Act, that is, the amount that a willing buyer of an asset could reasonably be expected to pay to acquire the asset from a willing seller if the following assumptions were made:

- that the buyer and seller dealt with each other at arm's length in relation to the sale;
- that the sale occurred after proper marketing of the asset;
- that the buyer and seller acted knowledgeably and prudentially in relation to the sale.

SMSFs were generally able to choose either the historical cost or market valuation accounting method to value their assets when preparing their financial statements. SMSFs paying a pension or those with in-house assets are currently required to value assets at market value each year.

Subsection 35B(5) provides that a person commits an offence if the person contravenes section 35B and carries a penalty of 100 penalty units.

Subsection 35B(6) provides that this is also an offence of strict liability and carries a penalty of 50 penalty units. An offence of strict liability is an offence for which there are no fault elements for any of the physical elements of the offence and the defence of mistake of fact is available (section 6.1 of the *Criminal Code Act 1995*).

## **Statement of Compatibility with Human Rights**

*Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011*

### **Superannuation Industry (Supervision) Amendment Regulation 2012 (No. 2)**

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

#### **Overview of the Legislative Instrument**

The purpose of the Legislative Instrument is to require trustees of self managed superannuation funds (SMSFs) to consider insurance for members as part of the fund's investment strategy; keep money and other assets of an SMSF separate from those held by a trustee personally and by a standard employer-sponsor or an associate of a standard employer-sponsor; and require SMSF assets to be valued at market value for reporting purposes.

#### **Human rights implications**

This Legislative Instrument does not engage any of the applicable rights or freedoms.

#### **Conclusion**

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.