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Discussion Paper

10 smart ideas to better manage your SMSF

This discussion paper is not intended to be taken as advice to buy or sell a particular financial product. The information contained here is of a general nature only.

For many people superannuation is their only retirement nest egg. For most it is the largest asset outside of the family home. So it is within this context that self managed superannuation continues to play a significant role.

Around 855,000 Australians are Trustees of their own superannuation fund. Self managed funds now hold around one-third of Australia's total superannuation assets. At June 2011 this was over $430bn. The average balance is now around $960,000.

As Trustee of the Fund you bear the ultimate legal responsibility for the Fund. Even more importantly, it's your future – it's important not to get it wrong. While the ATO has been quite successful in changing the common name from 'DIY' (and hence the *do-it-yourself* perception) to 'SMSF', a better approach is to think of it as your own '**private fund**'.

Superannuation is a complex area and investing in it, no less so. So with this in mind, how can you better manage your Fund?

1. Be diligent with the Fund's paperwork

We suggest to clients that they have 2 files:

i) **A working file** - for tax statements, dividend advice or documents that specifically relate to that tax year. This is then updated annually with the prior year filed with the completed tax returns.

ii) **A permanent file** - holding the Fund's trust deed (and any amendments), the investment strategy, minutes, asset register and the like.

It is a legislative requirement that minutes and records are kept for 10 years. The same requirement applies to a change in Trustee. Accounting records must be kept for 5 years. The trust deed and any superseded versions must always be retained.

2. Document what you do and why you have done it

The ATO continues to highlight that documentation is an area that needs to be improved by Trustees. Documentation is essentially an audit trail. Yes for your accountant, but more importantly for you. What is clear to you at the time you do it is often obscured by the passing of time. Hence detail what you do and why in a clear manner for later reference.

If it helps, hold 20 or so bound pages in your file to allow you to easily document decisions and actions as you take them.

3. Consider a software package to track investments and income

There is good software available to do this, but again it involves a little bit of effort. See what software will assist your accountant in preparing the Fund's accounts, as this will likely save you on compliance costs.

Via a financial adviser some financial planning software can allow client access to their (total) portfolio. This is true of Xplan, the system we use.

This can then be used as the asset register for the Fund.

4. Regularly update the Fund's trust deed

Look upon this as simply a (minor) running cost of the Fund. Generally a deed should be amended every couple of years or where there has been significant changes to the legislation where it impacts you as the member. For a couple of hundred dollars, it makes sure you are operating under the latest rules and is money well spent.

It is also a very good idea to read your deed – understand what can and cannot be done - as Trustee legal responsibility ultimately rests with you.

5. Keep things simple

Have one central bank account, where all income and expenses are received into and paid from*. Even better use an account where you can add in a narrative for each transaction (or simply add this information onto your bank statements).

It is not only easier for you to recollect what the entry is (in conjunction with the documentation outlined above), but it will also be clearer for your accountant. Often your accountant can be given access to this information electronically. Again this should help you save on costs.

Similarly hold your ASX shares on CHESS, with one broker. Issuer sponsorship is an inefficient way to manage a portfolio. While there is some attraction in dividend reinvestment plans (known as DRPs), the additional accounting required to track these small purchases, coupled with the unconscious decision to add to a stock, makes me favour simply receiving the cash dividend.

** This may vary where you are drawing a pension and the assets are segregated.*

6. The investment strategy is the Fund's business plan – use it as such

The Fund's investment strategy should be meaningful and measurable.

The temptation is to have a 1-2 page generic document that simply meets your compliance obligations if the ATO comes knocking. Instead look upon it as the *business plan* of the Fund: how you are going to manage the Fund's assets, given critical issues such as return and risk, diversification, liquidity, cash flow etc to achieve the Fund's stated objectives.

One area that is almost never dealt with well, if at all is the issue of risk management within a portfolio. It should be more obvious now that markets are not always efficient as people are not always rational.

So hence do not expect that a set-and-forget investment strategy will cope under all market conditions. Professional money managers have risk constraints over their portfolio holdings for at least two good reasons:

i) It is a governance requirement *(and it is for you)*

ii) No matter how much you think you know an investment or a business, the future is always unknown and hence returns are variable

We would suggest the list of questions to think about includes:

i) Should there be limits on what percentage of the portfolio is invested?

ii) Should there be limits on how much is held in each stock and sector?

iii) What is a realistic assessment of your own abilities and hence how this impacts your investment strategy and approach?

iv) Should there be stop loss limits

v) If the approach in part or total is a *buy-and-hold* strategy – what are the implications of this that need to be thought through?

The investment strategy should be a living document that you finesse over time to reflect your own personal strategy – as it evolves and as your personal circumstances, or economic and market conditions dictate. An investment strategy should be based on an investment philosophy – your core beliefs about investing.

If you cannot clearly, specifically and sensibly articulate your investment philosophy and strategy, to another person in 3-5 minutes then you need to give it far more thought.

7. Think about what happens if you die or are disabled

The inescapable reality is that we will all die some day. We just don't know when. An adage to follow is "*plan as though you will live to 100, but prepare as though you will die tomorrow*".

It is also not just about death. Disablement, in its many forms, may be more of a problem for a Trustee. This raises some practical questions that need consideration including:

i) Who will run the Fund if you are not able to? Who is your legal personal representative (executor / power of attorney holder) and what skills do they have?

ii) Do you need to execute a binding death benefit nomination?

iii) Who will receive your benefits on death and how?

iv) Will benefits need to be paid out from the Fund – will it impact the assets held?

v) How flexible is your Will, especially in being able to deal with super assets?

As a part of your estate plan, document where the Fund's records are kept, who are the main advisers to the Trustees and their contact details and the like. This may be best kept with your estate planning documents – which may be provided as a comprehensive package by a specialist estate planning lawyer.

8. Make sure all the Fund's assets are held in the name of the trustee

In most cases the assets of the Fund will be held as XYZ Pty Ltd as trustee for XYZ Superannuation Fund.

In some instances this is not possible (e.g. real estate). Therefore a declaration of trust should be completed to acknowledge that the asset belongs to the Fund. Without this then the ownership of the asset becomes contentious. It is also something the ATO is very particular about.

One advantage of a (sole purpose) corporate trustee is the distinction it places between the members and the assets. It also easily allows changes to be made to the members of the Fund. There are also other advantages of a corporate trustee.

9. Education

Just as you probably did when you were first considering a SMSF, learn. Continue the learning journey. The area of SMSF is very broad and touches on specific legislative and regulatory requirements, but there is also the pragmatic side: you are managing your own retirement pool. Take a business-like approach. It's too important to do otherwise.

10. If in doubt ask

It is far simpler to find a solution to an issue than to undo a problem once created. Generally it is far less costly as well (*'an ounce of prevention is worth a pound of cure'*).

The Fund's accountant, auditor or specialist adviser can assist you in this regard.

Summary

I hope that this helps you better understand key considerations for managing your own superannuation fund.

At every point think to yourself – if someone had to come along and run the Fund in my absence, would they be able to understand what has been done?

SMSF: Too important to get wrong; too easy to get wrong.

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