THOMSON GEER
LAWYERS

ADVICE | TRANSACTIONS | DISPUTES
Domestic & Cross Border

SHIFTING GEER AUGUST 2014

26 AUGUST 2014

Welcome to Shifting Geer, Thomson Geer's superannuation newsletter for the period 28 July 2014 – 22 August 2014.

APRA AND ASIC UPDATES

ASIC Statement on wholesale and retail investors and SMSFs
(8 August 2014)

ASIC has clarified how it will apply the wholesale investor test to self-managed superannuation funds (**SMSFs**). ASIC now considers that any SMSF holding assets worth at least $2.5 million (rather than $10 million), as certified by a qualified accountant, would be considered to be a "wholesale client" for the purposes of *Corporations Act*, section 761G.

Given that many SMSF members may have invested up to $1 million in non-concessional contributions in the 2007 Financial Year (probably via the transfer of commercial property) on top of any other contributions over the years, it is likely that many SMSFs could fall within the meaning of "wholesale client".

Thomson Geer comment: *It is important for service providers to remember that they must obtain evidence, via a qualified accountant's certificate, that the SMSF trustee would be a wholesale client before treating such a client as a wholesale client (i.e. by failing to provide some of the statutory protections afforded to retail clients) and ASIC states that it will take regulatory action where financial service providers miscategorise their clients.*

APRA Reporting Framework FAQs
(11 August 2014)

APRA has issued the following Reporting Framework FAQs:

Defined benefit reporting

FAQ 104: Does all of the information reported under item 1 of Reporting Form SRF 160.0 Defined Benefit Matters (SRF 160.0) need to be as at the same date?

Abridged answer: Yes, these items are to be reported as the most up to date information available to the trustee as at the end of the reporting period, where all four items 1.1 to 1.4 were calculated as at a consistent point in time.

For example, if a trustee is required to complete SRF 160.0 as at 30 June 2015 and it has available the following information at the following dates:

- Item 1.1 – accrued benefits – as at 30 June 2013 (actuarial investigation) and 30 June 2014 (estimate);
- Item 1.2 – vested benefits – as at 30 June 2013 (actuarial investigation), 30 June 2014 (estimate), 31 December 2014 (estimate) and 30 June 2015 (estimate);

- Item 1.3 – minimum benefits – as at 30 June 2013 (actuarial investigation) and 30 June 2014 (estimate); and
- Item 1.4 - Net assets available for members' benefits (net of ORFR reserves) - as at 30 June 2013 (actuarial investigation), 30 June 2014 (estimate), 31 December 2014 (estimate) and 30 June 2015 (estimate),

the trustee must report items 1.1 to 1.4 as at 30 June 2014, as this is the most recent consistent date of the information required.

Insurance

FAQ 99: Must an RSE licensee report insurance related flows on Reporting Form SRF 330.1 Statement of Financial Performance (SRF 330.1) and Reporting Form SRF 330.2 Statement of Financial Performance (SRF 330.2) in accordance with the fair and reasonable allocation processes required under s 99E of the SIS Act?

Abridged answer: No, a trustee should report in the manner that the insurance-related flows operate in practice. The fair and reasonable allocation requirements under SIS, section 99E apply only to reporting of superannuation activities (items 3 to 7).

APRA recognises the practical demarcation of superannuation activities and insurance activities within a typical fund. Therefore insurance related flows are not subject to the fair and reasonable allocation requirements under SIS, section 99E.

However, where insurance occurs at the member level, apportionment may be required. In this circumstance, APRA expects insurance related flows to be reported in accordance with the manner in which premiums are deducted from the member's account in practice.

For example: a member holds interests in both a MySuper account and choice account within a fund but the trustee or member has determined that 100% of the member's insurance premium will be deducted from the member's MySuper account. Report about all of the insurance related flows in respect of this member on SRF 330.2 (MySuper), to reflect actual practice.

SRF 331.0

FAQ 100: Must an RSE licensee report about all services undertaken on Reporting Form SRF 331.0 Services (SRF 331.0)? Should an RSE licensee apply a materiality threshold to items reported on this form?

Abridged answer: Yes

APRA considers that there is scope for a trustee to apply judgement in determining whether a particular service is undertaken with respect to a fund or not. Where a service is provided, but it does not affect the fund's operation, APRA considers it reasonable for a trustee not to report this service on SRF 331.0.

For the avoidance of doubt, all material outsourcing activities must be reported on SRF 331.0.

Illustrative examples:

- the engagement of a technician to repair photocopying equipment used by trustee staff could be excluded from reporting because the fund is not impacted by this arrangement; and
- a trustee engages an actuary to undertake a one-off asset-liability modelling exercise in respect of the fund. The service provided by the actuary is one-off in nature and the engagement is not on a continuing

basis and is not a material outsourcing arrangement. Despite this, the trustee recognises that the actuary has been engaged to provide services with respect to the fund and it reports this arrangement.

FAQ 101: How must an RSE licensee report multiple services provided under one arrangement in items 1 and 2 of Reporting Form SRF 331.0 Services (SRF 331.0)?

Abridged answer: Where the trustee, or an external service provider provides multiple services with respect to a fund, the trustee must report each type of service, split by role type, on separate rows in items 1 and 2 of SRF 331.0.

In practice, this means the trustee must:

- complete all line items in respect of each role performed by the trustee or service provider;
- where possible, report the expense associated with each role. Where an explicit breakdown of expense is not available, it is APRA's expectation that the trustee should apportion the expense by role type on a basis that it considers reasonable; and
- (in respect of an external service provider) if a trustee is not able to apportion the expense by role type on a basis that it considers reasonable, report the entire expense associated with that external service provider in the row that corresponds to the primary service provided. Report zero expense in each of the other rows for this service provider, to avoid a mandatory D2A validation.

Investments Reporting

FAQ 103: How are RSE licensees required to report counterparty credit ratings to APRA on Reporting Form SRF 532.0 Investment Exposure Concentration (SRF 532.0) and Reporting Form SRF 534.0 Derivative Financial Instruments (SRF 534.0), when directly held debt investments, or counterparties to over-the-counter derivative contracts, have been rated by more than one credit rating agency?

Answer: APRA requires RSE licensees to report counterparty credit ratings for "directly held investments – large exposures", in item 1, column 8 on SRF 532.0. In addition, APRA requires RSE licensees to report counterparty credit ratings for counterparties to over-the-counter derivatives contracts in item 4, column 2 on SRF 534.0. The counterparty credit ratings, used for the purposes of APRA reporting requirements, are generally consistent with long-term credit ratings provided by credit rating agencies.

APRA's reporting instructions state that where an RSE has an investment with multiple ratings from two or more credit rating agencies, the RSE licensee must consistently apply the lowest rating where the individual ratings conflict. The reporting instructions do not require an RSE licensee to solicit credit ratings from each of the credit rating agencies which provide a rating on that particular investment or counterparty. If the RSE licensee has only solicited credit ratings from one credit rating agency, then the credit rating from the single ratings agency is to be used to determine counterparty rating grades to be reported to APRA.

Where an RSE licensee has solicited credit ratings from multiple ratings agencies, the RSE licensee must consistently apply the lowest:

- issuer credit rating awarded by the credit ratings agencies, whenever the individual ratings on a directly held debt investment, conflict. The issue credit ratings will be used for the purposes of reporting to APRA in item 1, column 8 on SRF 532.0.

- issuer credit rating awarded by the credit ratings agencies, whenever the individual ratings on a counterparty to an over-the-counter derivative contract, conflict. The issuer credit ratings will be used for the purposes of reporting to APRA in item 4, column 2 on SRF 534.0.

Profile and Structure

FAQ 102: Noting APRA's ongoing consultation on the reporting requirements for select investment options, should I still complete item 6.2 of Reporting Form SRF 601.0 Profile and Structure (RSE) (SRF 601.0)?

Abridged answer: Yes. Item 6.2 of SRF 601.0 must be completed with reference to the existing definition of a select investment option, set out in the Interpretation section on pages 6 and 7 of the instructions to SRF 601.0.

APRA has temporarily removed the requirement to report select investment options on Reporting Form SRF 001.0 Profile and Structure (Baseline) which is used to allocate the correct reporting forms to each trustee within D2A.

However APRA still requires trustees to report information in respect of select investment options, under the existing definition, under SRF 601.0.

Changes to the select investment option reporting requirements are expected to take effect from 1 July 2015.

APRA has also issued the following Prudential Practice Guides FAQ:

FAQ 4: How should funds under management (FUM) be determined for the purpose of calculating an ORFR target amount?

Abridged answer: FUM for this purpose should be determined as net assets available to pay members' benefits.

APRA has identified an error in Prudential Practice Guide SPG 114 Operational Risk Financial Requirement (SPG 114) under paragraph 9, which states:

"For the purposes of calculating the ORFR target amount, APRA views FUM as the total of asset balances of each RSE within the RSE licensee's business operations."

This paragraph should refer instead to "the balance of net assets available to pay members' benefits".

APRA will amend the SPG 114 in due course, to accurately reflect the correct reference.

APRA has amended the following Reporting Framework FAQs:

Defined benefit reporting

FAQ 23: Are Reporting Form SRF 160.0 Defined Benefit Matters (SRF 160.0) and Reporting Form SRF 160.1 Defined Benefit Member Flows (SRF 160.1) to be reported for each sub-fund as well as each defined benefit RSE?

Insurance

FAQ 86: What amount must be reported in Reporting Form SRF 161.0 Self-Insurance (SRF 161.0) or Reporting Form SRF 250.0 Acquired Insurance (SRF 250.0), for income protection insurance cover and claims?

SRF 330.0

FAQ 44: Some data items in Reporting Form SRF 330.0 Statement of Financial Performance (SRF 330.0) are not currently captured in

an RSE licensee's systems. How should these be reported before the implementation of the SuperStream Data and Payment Standards?

Investments Reporting

FAQ 60: Where an indirectly held investment contains derivative contracts, how should those derivative contracts be reported on Reporting Form SRF 530.1 Investments and Investment Flows (SRF 530.1) and Reporting Form SRF 530.0 Investments (SRF 530.0)?

FAQ 97: How should an RSE licensee incorporate derivative exposures when reporting directly held and indirectly held investments on Reporting Form SRF 533.0 Asset Allocation (SRF 533.0)?

SRF 700.0

FAQ 75: How should an RSE licensee that currently uses an investment objective expressed as a percentile of the distribution (e.g. 25th percentile) report their return target on the MySuper product dashboard (per the requirements in Reporting Standard SRS 700.0 Product Dashboard (MySuper) (SRS 700.0))?

LEGISLATION

Superannuation Industry (Supervision) Amendment (Pass Through of Employee Details) Regulation 2014

(Draft released 1 August 2014)

Treasury released the exposure draft Regulation which proposes to amend the SIS Regulations so that, from 1 July 2015, a default fund of an employer that receives contributions data which relates to another superannuation fund must pass the contributions data on to the correct fund.

The effect of this is that each fund that offers a MySuper product must provide a service so that an employer who has chosen the fund as their default can deliver all contributions data to a single location and be certain that all data will be routed to the right destination, whether that is the default or any other superannuation fund (pass-through).

A number of default funds already provide a similar service via a data and payment clearing service offered to employers.

A default fund offering a transitional "portal" solution that does not currently have the capacity to ensure the delivery of all of a default employer's contributions (including that relating to other superannuation funds), will be required to:

- develop such a service; or
- outsource the delivery of such a service to a third party provider; or
- facilitate and encourage the use of data clearing via their nominated gateway provider with direct payments by the employer to target funds.

This may be achieved by including a clearing capability in the portal or by means of an alternative service that allows a default employer to deliver contributions data to a single location from which it is routed to the correct fund.

The closing date for submissions is Monday, 1 September 2014.

CASES

There were no cases of interest for this period.

OTHER RECENT DEVELOPMENTS

ATO Interpretative Decision ATO ID 2014/27 Superannuation contributions tax - contributions and surcharge liability

(15 August 2014)

The ATO has released its Interpretative Decision stating that payments made by a member to an unfunded defined benefits provider in respect of surcharge payable under the *Superannuation Contributions Tax (Assessment and Collection) Act 1997* (**SCTA**) are not to be regarded as contributions made to obtain superannuation benefits.

Decision

The ATO has formed this view on the basis that member payments are made to the provider under subsection 16(7) of the SCTA for the purpose of reducing the amount by which the member's surcharge debt account is in debit and are not contributions made by the member to the provider for the purpose of obtaining superannuation benefits.

Reason for decision

SCTA, section 16 makes provision for the deferment of the liability of an unfunded defined benefits provider to pay surcharge assessed as payable on a member's surchargeable contributions for a financial year.

The unfunded defined benefits provider is required to keep a surcharge debt account for each member and debit the account for surcharge assessed to be payable on the member's surchargeable contributions. If the member's account is in debit at the end of a financial year, the provider is required to debit the account for interest.

Subsection 16(7) of the SCTA operates to allow a member to make payments to the provider for the purpose of reducing the amount by which their surcharge debt account is in debit. A specific subsection of the fund's governing rules allows a contributor '*...to pay amounts to the fund in respect of the superannuation contributions surcharge payable in respect of the contributor*'.

A member payment received by the fund provider pursuant to subsection 16(7) of the SCTA, and permitted by the specific subsection of the fund's governing rules, is an amount paid to the fund for surcharge payable in respect of the contributor. The provider is required to forward the payment to the Commissioner of Taxation. Accordingly, the payment does not take on the characteristics of a contribution to obtain superannuation benefits but is clearly a payment made to reduce the balance of the member's surcharge debt account.

In addition, the fund's governing rules require the fund to refund to the member, any such payments that are received which are in excess of the member's surcharge debt account. This means the excess payments do not result in additional pension benefits and do not remain in the fund. Accordingly, the amounts are not contributions to obtain superannuation benefits but are member payments specifically made to the fund pursuant to subsection 16(7) of the SCTA to reduce surcharge payable in respect of the member's surchargeable contributions.

WRITTEN BY:

Mark Abramovich | Partner | +61 3 9641 8627 | mabramovich@tglaw.com.au
Luke Hooper | Senior Associate | +61 3 9641 8767 | lhooper@tglaw.com.au

SYDNEY
Level 25
1 O'Connell Street
Sydney NSW 2000
+61 2 8248 5800

MELBOURNE
Level 39
Rialto South Tower
525 Collins Street
Melbourne VIC 3000
+61 3 8080 3500

MELBOURNE
Level 20
385 Bourke Street
Melbourne VIC 3000
+61 3 9670 6123

BRISBANE
Level 16
Waterfront Place,
1 Eagle Street
Brisbane QLD 4000
+61 7 3338 7500

ADELAIDE
Level 7
19 Gouger Street
Adelaide SA 5000
+61 8 8236 1300

www.tglaw.com.au