

# Chan & Naylor: Initial Submission to the Financial System Inquiry

2014

## Introduction

Recognising that this as a once in a generation chance to “establish a direction for the future of Australia's financial system”, Chan & Naylor welcomes the opportunity to provide input into the Governments Financial System Inquiry (FSI).

As Australia's fastest growing accounting firm Chan & Naylor is a holistic provider of financial advice and accounting services for individuals, small business and property investors. With a national presence in metropolitan, suburban and regional Australia Chan & Naylor has a clear understanding of the financial pressure points and short falls that adversely impact many ordinary Australians. Chief among these is a lack of industry regulatory governance along with low financial literacy among ordinary Australians.

To this end, the specific topics within the FSI's terms of reference that Chan & Naylor would like to address are:

- Balancing competition, innovation and efficiency with stability and consumer protection;
- The effectiveness and need for regulation;
- The role of Government and financial regulators; and,
- Promoting a competitive and stable financial system that contributes to Australia's productivity growth through improved financial literacy.

### 1. Restoring The Fiduciary Client Relationship

Regrettably when it comes to providing excellence in client advice both the financial services and accounting industries have in Chan & Naylor's opinion 'missed the boat'.

The former industry has been closely scrutinised and even penalised over the years, whilst the latter has simply failed to step up to the plate, which is troubling given that accountants enjoy one of the closest and most trusted of client relationships of any profession.

And whilst the financial services industry has arguably been too forward looking, the accounting industry has been too backwards looking. Meanwhile the insurance sector has been allowed to morph itself into the financial advice profession as the Australian financial system itself has been blind-sided by hidden agendas, conflicted interests and ineffectual financial literacy standards.

Until these discrepancies are resolved it is the consumer who will bear the brunt of an industry short fall. Put simply, the financial sector has dropped its duty of care to Australian consumers.

The intent of any reform is to never lose sight of who this service is for, and in the case of the FSI Chan & Naylor believes that we now have an opportunity to restore the fiduciary client relationship.

### The Fix

Australia requires a cross industry level playing field ruled by a common standard of corporate governance, education (both for industry and consumer) and ultimately one regulatory authority overseeing the collective investment industry.

By example there is no recourse on the real estate industry should a \$1m off the plan property investment sour. This is not the case for financial planners or dealer groups. Whereas the Australian Securities and Investments Commission (ASIC) controls dealer groups, planners and manufacturers, who is controlling the real estate agents, mortgage providers, banking sector and self-managed super fund (SMSF) providers?

Chan & Naylor recommends that ASIC should be at the forefront in upholding a widely recognised standard and code of conduct that provides clear and consistent compliance guidelines for all areas of investment and related advice.

Having a single set of industry rules with one common outcome will enable the industry to act in the best interests of its clients and achieve the best outcome on their behalf.

### **What Is the Alternative?**

If a common standard is not achieved then the financial services sector risks becoming an even more disjointed environment, allowing the unscrupulous to fly under the radar and prey on vulnerable consumers. This will necessarily require ASIC's reactive response to put out spot fires and rule with an iron fist rather than educational agenda.

The question is, how many Storm Financial or Trio Capital collapses does Australia need before we realise that self-regulation is not working for the common good?

## **2. A National Solution to Address Consumer Financial Illiteracy**

In addition to fixing industry, Chan & Naylor is also concerned with the lack of consumer education and understanding of increasingly sophisticated financial products, such as SMSFs, that Australians are increasingly exposed to.

With the FSI again comes the opportunity to address the issue of financial illiteracy through a comprehensive industry based education program that will better prepare and protect Australians against the unscrupulous and mistakes caused by lack of knowledge, particularly around compliance rules and guidelines.

In light of the current property cycle upswing and the growing attraction of SMSFs, the term 'property spruiker' has had significant airplay within the media recently. The concept however is not new or limited to property investments alone, as ill-advised share and derivatives investments have also caused problems in the past for investors.

Chan & Naylor believes that the popularity of SMSFs will continue to grow and that this form of independent retirement vehicle should be applauded and encouraged. However we also believe that urgent action is required to create and manage a national educational framework established with the principal aim of educating the general public on the merits and potential pitfalls of SMSF investments, thereby minimising future risk from aggressive selling practices and distortions within investment markets.

In representing a significant number of 'mum and dad' SMSF investors Chan & Naylor acknowledges that it is the public's own responsibility to invest in their own financial knowledge and understanding. However as retirement mechanisms become increasingly complex, we now believe that there is urgent need for the establishment of an independent body that provides balanced and up to date information along with unbiased opinion.

Chan & Naylor recommends that this independent national financial education body would be best served by an industry collective that is led by the Australian Securities and Investments Commission (ASIC).

Through extensive experience of assisting trustee holders whom have experienced mixed SMSF advice in the past and given the surging interest in this trust based mechanism, Chan & Naylor believes that there is no better time to address the nationwide 'financial knowledge gap' head on before major adverse problems arise. Preventative action ahead of remedial action in such a sensitive and major Australian economic sector must be the preferred course.

Whilst industry compliance within this sector is generally good, the difficulty is that many first time SMSF investors need to carefully consider any investment decision as well as be wary of breaching ATO rules, which are complex in this area. The public need to be educated on the various responsibilities they as the investor must shoulder and how to ask the right questions and from whom to get information and advice that suites their needs.

While the Future of Financial Advice (FoFA) reforms would have gone a significant way to achieving this it still would not have been specific enough to manage the SMSF sector as many Australians try and do it all themselves and then fall foul of either regulatory mishaps or are taken in by the notion of easy success.

The ATO recently described property investments in SMSF as a 'problem child' because of its fears that low-interest rates, tax breaks, property spruikers and rising prices were encouraging reckless investments. Chan & Naylor agrees that the ease of entry into the SMSF market combined with a lack of current unbiased information or ill-informed advice is problematic.

With Generation X generating dramatically more superannuation contributions than their Baby Boomers parents, this issue will continue to grow and as such the industry as a whole has a responsibility to ensuring that their clients are up to speed with current rules and regulations as well as trends which drive the SMSF sector. Previously such a response was not required because people could not access their super until their retirement. This has clearly now changed in that people can have a say in their investments and can pool family resources. The general lack of confidence in the overall superannuation and equities industry just serves to exacerbate the issues.

### **Filling the Gap: the Role of ASIC**

Super access is a cyclical honey pot problem and fixing it requires better-informed participation by SMSF trustees.

Presently, aside from what the public read in the media, the only consumer advice available is through the Australian SMSF Members Association (ASMA), via the commercial provider or through financial advisors or accountants (although both the latter are becoming increasingly regulated because of the proposed new FOFA laws). ASMA is not a dedicated consumer resource and the information made available is often subjective and insufficiently funded private organisation.

Chan & Naylor recommends that a new knowledge based resource be developed to provide up to date guidelines and an education framework that the that the general public can to go to in order to seek answers and generate appropriate and informed questions for their SMSF advisors.

The consumer advocacy group Choice provides an online consumer goods advice and information forum. A similar forum that is kept regularly up to date and is solely dedicated to the SMSF sector would a be a positive step towards filling the financial knowledge gap identified.

As Australia's existing corporate, markets and financial services regulator, Chan & Naylor believes that ASIC, with industry support, is the most appropriate organisation to lead such a forum to help inform, educate and alert the general public on what they need to know and understand about SMSFs. It also has the legislative framework to encourage and enforce compliance and education, the latter being also part of its charter.

ASIC's role of regulator for the broader investment landscape better positions it to undertake this role as opposed to the Australian Taxation office which are primarily responsible for SMSF regulation and revenue collection and ASIC is better situated to work with APRA who has the administrative responsibility over the non SMSF superannuation industry. The issues covered and addressed through this new education body under ASIC would allow spill over to all superannuation members not just trustee. This may even help retain the outflow from the industry/retail funds into SMSF's.

### **Approach**

Having recently released the 2014-2017 National Financial Literacy Strategy, ASIC is an active proponent of consumer financial education and already has a dedicated consumer website (Money Smart) which has the potential to host the proposed SMSF forum.

Chan & Naylor acknowledges that ASIC has a broad remit, which includes ensuring our financial markets operate in a fairer and more transparent manner. Undoubtedly this helped lead to better investor confidence.

As an extension of this, Chan & Naylor suggests that the SMSF forum would be based on a similar model to the existing ATO's Consumer Advisory Panel ("CAP") but with the sole focus on consumer SMSF education. The driving force of this would be an amalgamation of a nucleus group under the umbrella of CAP that understands the everyday trustee expectations and requirements of SMSF.

As this is an evolving sector, such a group would be led by ASIC and assisted by the ATO and strengthened by the inclusion of representatives from professional bodies and organisations within the superannuation industry that are not. Ideally this would include specialist accounting firms that understand the grass root issues of entry-level SMSF investors.

This dedicated SMSF education group, under the auspices of ASIC's leadership, would provide the general public with the support and real-time information on current issues, concerns and solutions that would be allow more Australian's to comply within the ATO's guidelines and ultimately achieve their goal of enjoying an independent retirement income if only due to improved levels of understanding that could better shape their investment decisions.

Pending analysis of the success of the SMSF education group, other specialist groups that similarly fall under ASIC's leadership could also be considered to help improve Australia's overall level of financial literacy.

## About Chan & Naylor

Chan & Naylor is Australia's leading national property business tax accounting and wealth advisory group. Chan & Naylor's key point of difference is a personalised team-centric accounting service complemented by business advisors, wealth planners and finance strategists that are part of the national Chan & Naylor Group.

Established in 1990 by Edward Chan and David Naylor, the Group has 24 offices in 15 locations nationwide and offers its clients a complete suite of property accounting, asset protection and wealth creation strategies and services.

BRW ranked Chan & Naylor as Australia's fastest growing accounting firm in 2007, 2008 and 2013 and is now proudly ranked 39<sup>th</sup> largest accounting firm in Australia. The top 50 firm's revenue lifted 42.8 per cent to \$18.6 million with 15 per cent organic growth and 85 per cent through joint venture acquisitions of smaller firms.

Renowned as property investment experts and innovative leaders for accounting services and products, Chan & Naylor is the first and only accountancy firm to have successfully obtained a Product Ruling from the ATO (PR2011/15) for interest deductibility on borrowed monies to invest in a Trust.

Chan & Naylor is addressing industry consolidation and the growth of fewer, bigger sovereign players through its Joint Venture Partner program. The program, which is backed by the centralised research and systems of the National Group, provides clients in major metropolitan and regional centres with a consistent and holistic one-stop accounting and financial advice service.

Chan & Naylor's partnership program offers multiple benefits including: centralised marketing support, a proven operations system, outsourced IT, HR, regulatory support; access to CN Academy, expert financial planning and mortgage brokerage capabilities within the Group.

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