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Total Recourse

Managing Risk in Self Managed Super Funds

Total Recourse

Self Managed Super Funds come with unique flexibility but also unique risks. There are serious obligations on SMSF Trustees to appropriately consider the insurance needs of their members, and for SMSF's to manage the unique risks posed by substantial investment in illiquid assets. In this session we look at insurance strategies to appropriately manage risks in SMSF's, while considering estate planning through real life examples to build a framework for SMSF Insurance Advice.

Agenda

- 01 Self Managed Super Funds in Australia
- 02 Regulatory Considerations
- 03 The SMSF Trustee
- 04 Positioning SMSF Advice
- 05 Case Studies & Strategies
- 06 Summary & Opportunity

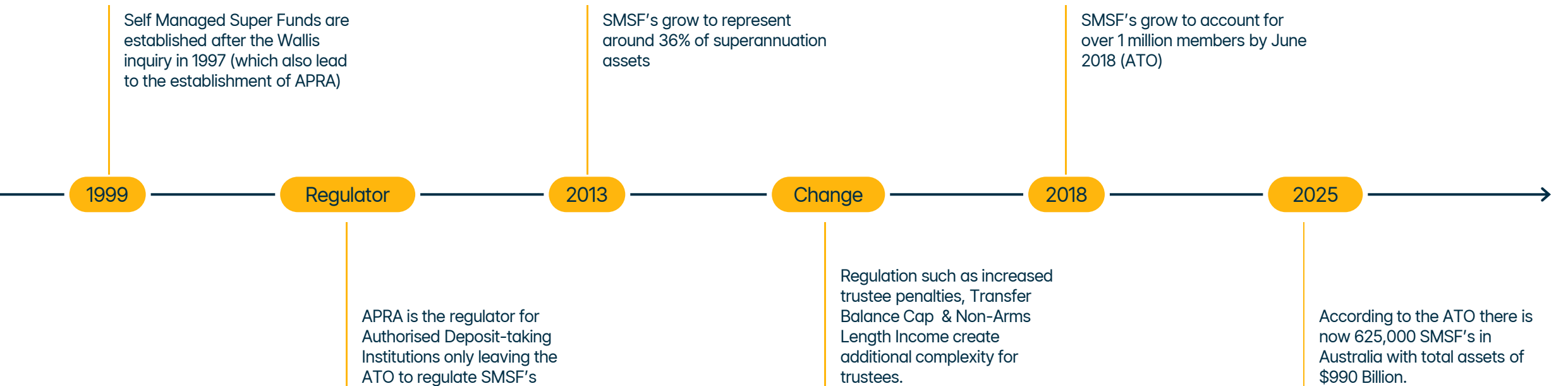


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01

Self Managed Super Funds in Australia

Self Managed Superannuation in Australia



Poll

According to the ATO, approximately how many SMSF's are there in Australia?

A. 500,000

B. 625,000

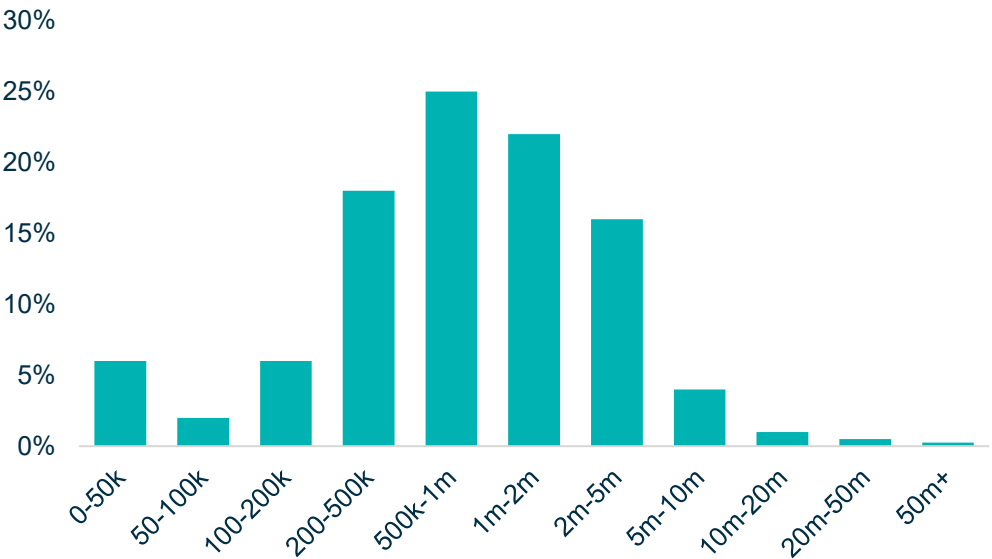
C. 390,000

D. 950,000

SMSF Size & Investments

Propotion of SMSF's by asset range

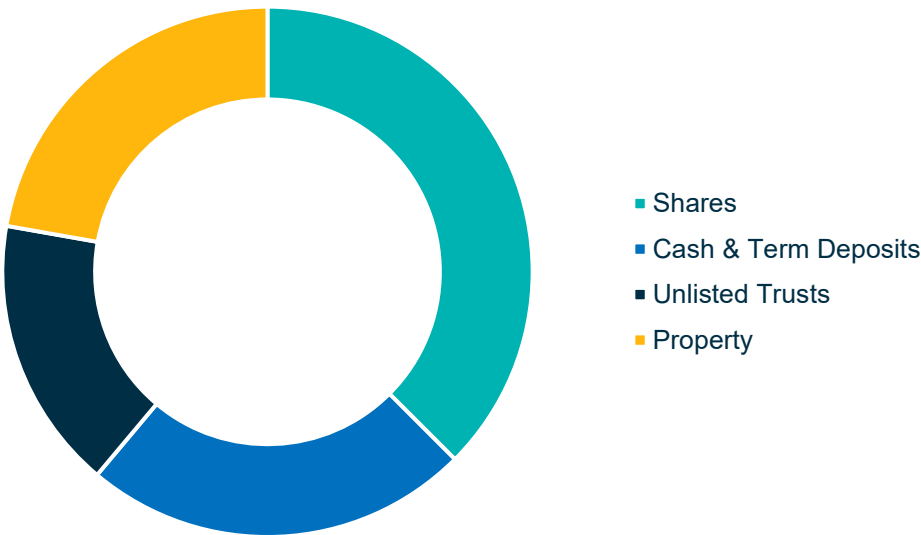
The majority of funds (65%) are between \$200k and \$2m balances, with the average being \$1.55m (\$835k/member).



ATO SMSF annual statistics 2023

Top 5 Investments

Property ranks almost an even second when it comes to popularity amongst SMSF assets.



ATO SMSF annual statistics 2023

Poll

What was the total asset value of these SMSF's?

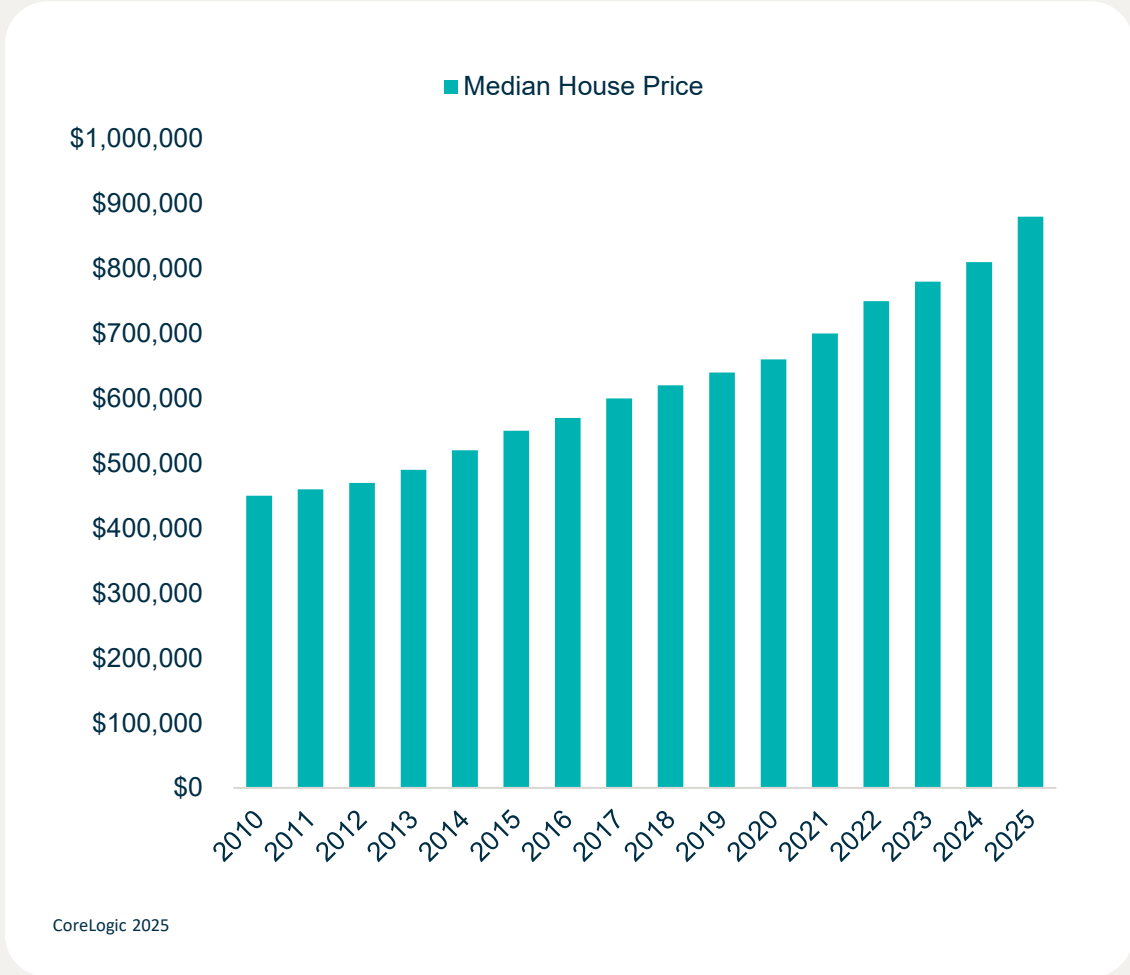
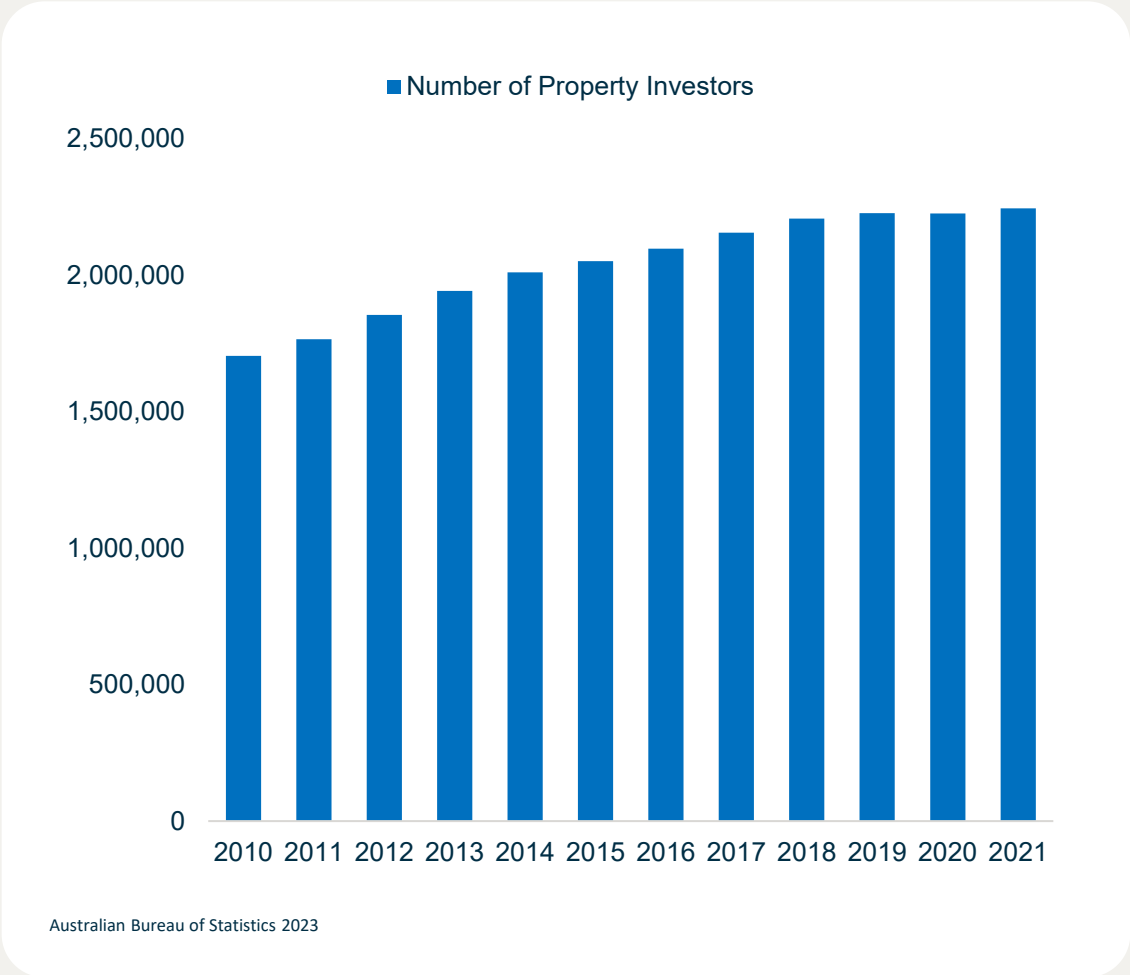
A. 990 billion

B. 880 billion

C. 900 billion

D. 750 billion

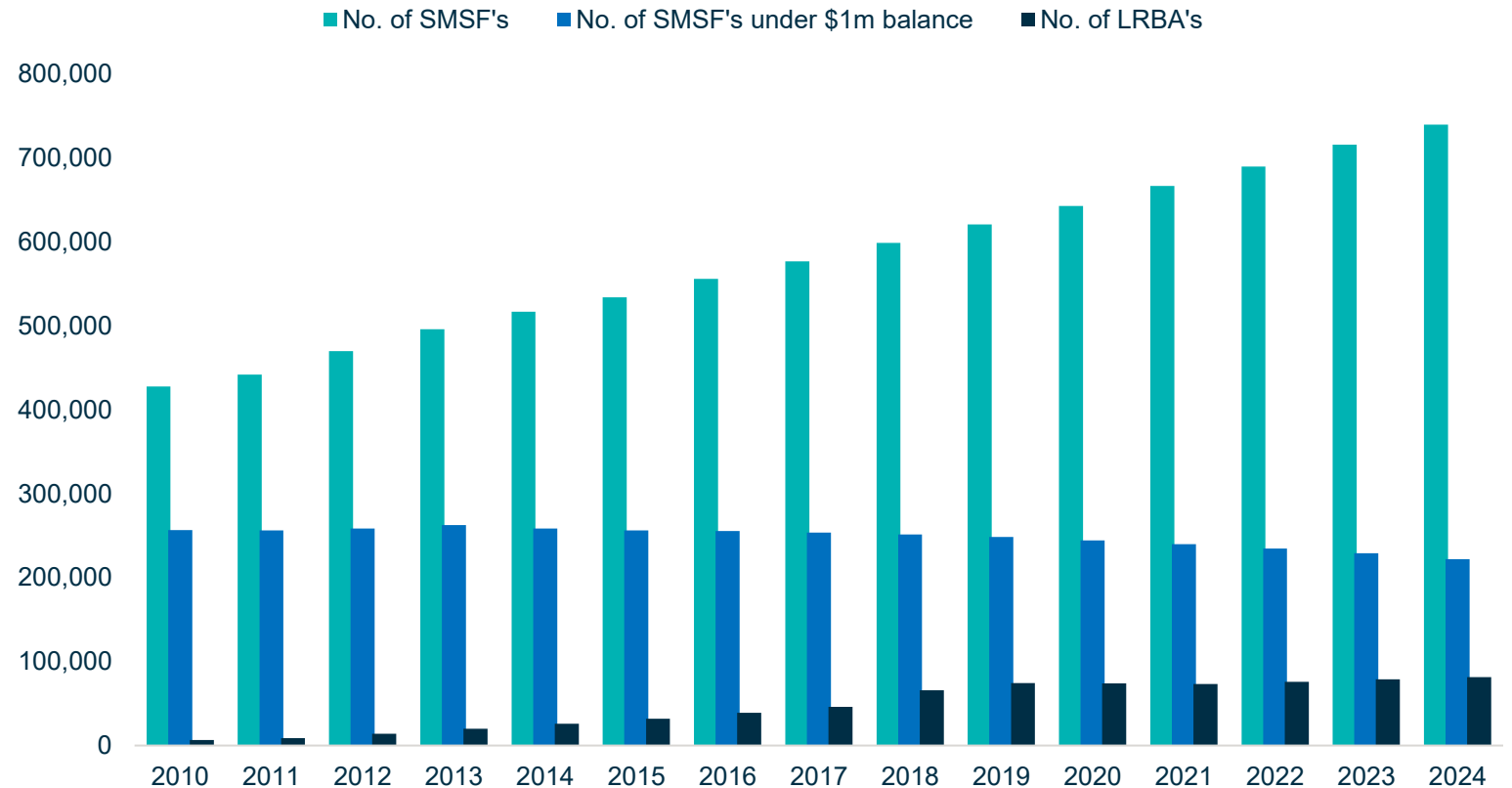
Australian Property Investment



SMSF's & Property

Using Superannuation to invest in Property

- More Australians have moved towards SMSF's and the appeal of direct control over investments.
- Numbers of SMSF's under \$1m have fallen proportionally – but is this in line with rising asset values as opposed to contributions and established holdings?
- Limited recourse borrowing arrangements and property have gradually become a larger part of SMSF investment strategies over the last two decades.



ATO SMSF Data – 2010 - 2024

SMSF's & Advice

A growth area

- Given the complexity of SMSF management, a surprisingly large portion of SMSF's are still managed directly.
- This creates a huge opportunity for advisers to engage with auditors and administrators to provide guidance to trustees on the management of their SMSF (including important risk management conversations).

53%

Of SMSF's are advised or held
on an advised platform

Intello, A State of the SMSF Market 2024

SMSF's & Succession

The demographics of SMSF's

- The member demographic of SMSF's tends to be older, and weighted further towards retirement
- This creates considerations when it comes to liquidity and cash flow requirements
- This creates potential exposures to death and disability
- This creates exposures on the continuity of the fund post event

65%

Of SMSF assets are in
retirement phase

63

Is the median age of all SMSF
members

ATO SMSF annual statistics 2023

Poll

What is the median age of all SMSF members?

A.60

B.61

C.62

D.63

SMSF's & Insurance

Risk Management in SMSF's

- Minimal uptake in insurance
- Many younger clients with accumulation needs and risk exposures
- Many older clients with potential health exposures and liquidity/income needs
- Many balances that would not support a member for their lifetime (including paying back debt)

13%

Take up rate of SMSF's and life insurance according to research by NobleOak.

20%

Of SMSF members are aged under 45 according to most recent ATO data.

43%

Of SMSF Member balances are under \$500k according to ATO data.

40%

Of SMSF members are aged 60 + according to the ATO.

Poll

What percentage of SMSF balances are under 500k according to ATO data?

A. 43%

B. 29%

C. 54%

D. 19%



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02

Regulatory Considerations

“

"SMSFs themselves aren't the problem. SMSFs as a superannuation vehicle are appropriate for a lot of consumers, but we really expect that when SMSFs are recommended to clients, it's very much based on their individual circumstances and considers what that particular vehicle is going to provide for those people".

Alexandra Sidoti, AFCA Senior Ombudsman for Investment and Advice

ASIC INFO274 SMSF Advice

Assessing SMSF Suitability

- The client must understand that outsourcing via professional advice does not absolve the trustee.
- The client must have time, skills, interest and experience to meet trustee responsibilities.
- Vulnerability and capacity of client.
- Future plans on residency and retirement
- Alternatives such as member directed investment facilities in APRA-regulated funds.



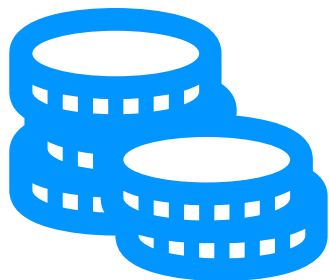
Insurance

- An SMSF trustee will need to consider whether to obtain and hold insurance cover for members and assets.
- Consider your client’s need for suitable and affordable insurance. In relation to their SMSF, you should consider and discuss with your clients:
 - their need for life, TPD, Income Protection, and
 - assets in the SMSF that may need insurance if applicable.
- If clients have existing insurance cover in their APRA-regulated fund, you must inform them of the costs and benefits of maintaining insurance cover through their existing fund - deciding not to hold any insurance or replacing existing insurance with a new insurance policy taken out by the SMSF.



Risks, Costs & Responsibilities

- Complaints against SMSF Trustees cannot be resolved through AFCA including trustee relationships & member death benefits.
- Legal costs & time on trust deeds
- Corporate trustee structures (according to the ATO over 70% of SMSF’s have a corporate trustee)
- Opportunity costs
- Administration and reporting
- Trustee succession planning & asset ownership



The Code of Ethics & AFCA Disputes

Key Standards

How does the Code of Ethics interact with SMSF advice and which key standards do we need to keep in mind?

Standard 3: Conflicts of Interest

Standard 5: Appropriateness (& Understanding) of Advice

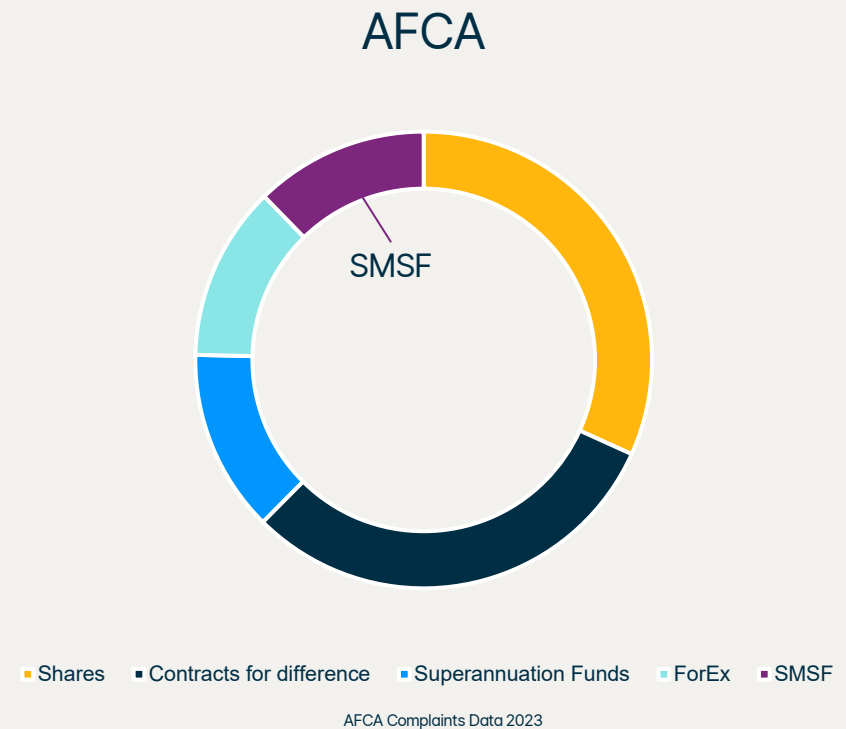
Standard 6: Likely long term broad considerations of advice

Standard 9: Products offered in good faith & not misleading

Standard 12: Rising tides lift all boats

Investment Advice Complaints

How often does SMSF advice come up in complaints at AFCA?



Risk Management & SMSF's



Often Overlooked

Benefits of flexibility, control and discretion over investments and tax are attractive, but the flip side is the lack of corporate infrastructure around risk management and member benefits.



Unique member profile

Both in number of members, age, and relationships between members (a key difference to an APRA fund)



Specialised Investment Decisions

Create unique risks when it comes to diversification and liquidity compared to the frameworks sitting around APRA funds.



Death Benefit & Succession Challenges

Managing payments, meeting member and beneficiary expectations and protecting family relationships create key risk management and regulatory issues for SMSF Trustees.

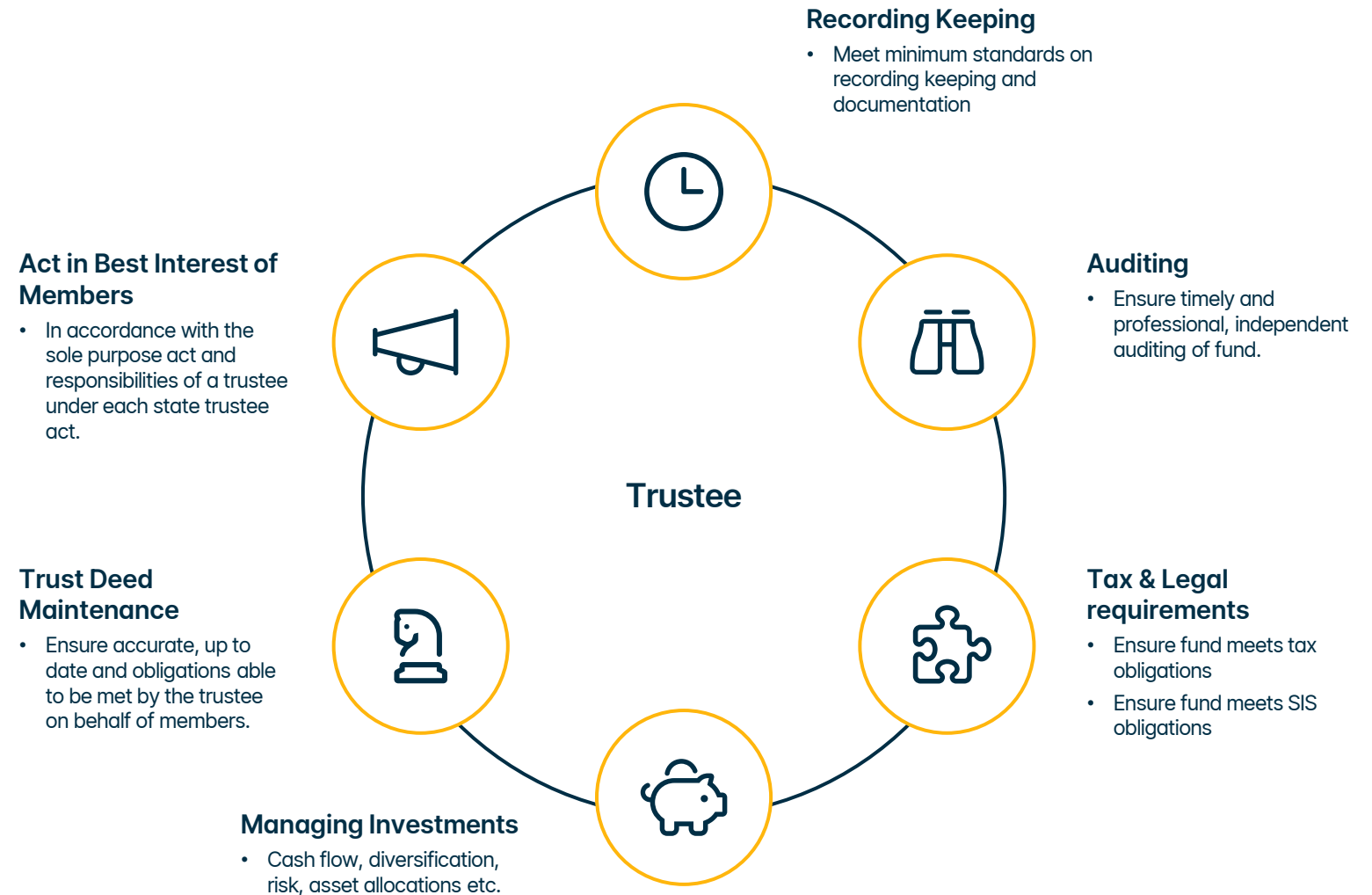


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03

The SMSF Trustee

The SMSF Trustee



Trustee Penalties

Breach	SIS Act	Penalty
Non-compliance with operating standards	34(1)	\$6,260
Financial accounts not prepared	35B(1)	\$3,130
Lends or provides financial assistance to a member or their relative	65(1)	\$18,780
SMSFs borrowings are non-compliant with legislation	67(1)	\$18,780
In-house assets rules not complied with	84(1)	\$18,780
Minutes of trustee meetings not kept for 10 years	103(1)	\$3,130
Elections in relation to pre-99 trusts not kept for 10 years	103(2A)	\$3,130
Records of changes to trustees not kept for 10 years	104(1)	\$3,130
Signed trustee declaration not kept for 10 years	104A(2)	\$3,130
Member/ beneficiary reports not kept for 10 years	105(1)	\$3,130
ATO not informed of significant adverse event	106(1)	\$18,780
ATO not informed that a superannuation fund has become or cease to be an SMSF	106A(1)	\$6,260
Trustee makes non-written appointment of investment manager	124(1)	\$1,565
Non-compliance with education direction	160(4)	\$1,565
Failure by new SMSF to give prescribed information to ATO within seven days	254(1)	\$1,565
Non-compliance with ATO request for statistical information	347A(5)	\$1,565

Managing Nominations of Beneficiary

A written nomination directing trustee to pay a members superannuation death benefits in a specific way

A valid binding beneficiary nomination removes discretionary elements that arise for trustees

Remove need for claim staking process and justification for discretion

Avoid potential conflicts and legal challenge (such as the LPR and Trustee being one and the same)

Ensure wishes of deceased carried out in the area of non-estate assets.

The funds governing rules are critical for validity of a binding nomination

Including:

- Fully complete fund document trail
 - Executed via wet signatures
 - Witnessed by two independent witnesses
- Complying with the rule of the SIS act

A BDBN *can* be indefinite (see Hill v Zuda Pty LTD 2022) however the funds governing rules may specify a time limit (such as three years). If ambiguous the court in the past has ruled the BDBN can only last 3 years (Donovan v Donovan 2009)

Reminder: Valid Beneficiaries

SIS Dependents (s10 SIS act 1993)	Tax Dependents (s302-195 ITAA97)
Spouse	Spouse or Former Spouse
Child (any age)	Child (under 18)
Interdependent Relationship	Interdependent Relationship
	Any other person who was dependant on the deceased before they died

Trustee's & Beneficiaries

Re Narumon Pty Ltd [2018] QSC 185 (Re Narumon)

- Member nominated 5% of superannuation to be paid to sister.
- Sister was not financially dependent and they were not in an interdependent relationship.
- Court ruled that the 5% request was not binding, and the trustee would deal with that 5% in accordance with the governing deed.
- This amount was then put back on the Trustee to justify and distribute the 5% in line with legal obligations.

The matter of Gainer Associates Pty Limited [2024] NSWSC 1138

- SMSF members husband and wife with no children, husband passed away in 2014 leaving wife sole member and director of corporate trustee.
- Wife formed a new relationship, with whom she listed in her will for cash, car, furniture, artworks and home.
- Signed a BDBN a week before she died, nominating LPR (but missing second witness signature – held to be invalid)
- NSW Trustee was surviving executor who appointed a liquidator to wind up SMSF and act as sole director
- After extensive process 1/3 was paid to the new partner, and 2/3 to her estate which was upheld by the courts.

Ioppolo v Conti [2013] WASC 389.

- Husband and Wife trustees & members of SMSF, wife had children from a previous relationship.
- Trust deed held that unless valid BDBN benefits would be paid at trustee's absolute discretion.
- Wife died, with no BDN but had expressed in her will that her superannuation were to be paid to her children and specifically stated it should not be paid to her husband.
- Husband left as sole trustee and appointed new corporate trustee which he was sole director and shareholder, directing the full benefit to himself.
- The children challenged unsuccessfully as their was no deed stipulation that the LPR become a trustee, and the will's contents does not legally cover superannuation.

Marsella -v- Wareham (No 2) [2019] VSC 65

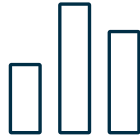
- Husband and Wife, Wife had 2 children from a prior relationship with the SMSF being her and her daughter (as members and trustees)
- BDBN no longer valid as had expired in accordance with the trust deed & named non eligible grandchildren
- The relationship between husband and children had also become strained and was the subject of an estate property dispute.
- Daughter appointed her brother as co-trustee, and paid the death benefit to the daughter and wound up the fund.
- The court ruled that the trustees had not given real and genuine consideration to the interest of the spouse & executor of the deceased, and did this in the context of substantial personal conflict with the husband.
- The children were removed as trustees, the beneficiary decision overturned and new submissions to new trustee taken.

Trustees & Insurance

August 2012: Following a federal government review, the SIS Regulations pertaining to investment strategies were amended to include reference to life insurance.

Specifically, trustees are now required by law:

To consider whether insurance cover should be held by the fund on the lives of the members, and to review that decision as SMSF trustees regularly as part of the review the investment strategy of the fund.



SIS Act 1993

s52B (f)

- i) Risks involved with investment decisions (including meeting cash flow requirements)
- iii) Liquidity of a funds investments
- iv) Ability of fund to discharge future liabilities



Sole Purpose Test

s62

- 1) a) iv) Provision of benefits on or after the members death
- b) ii) Provision of benefits on or after cessation of work on account of ill –health (whether physical or mental)

SMSF Trustee Risk Management Engagement



Identify

- The risk and what it represents to both the trustee and members.

Educate

- On the consequences of the risk eventuating and the likelihood of this occurring.

Quantify

- Attach a dollar figure to the potential impact this may have in costs (sale of assets/losses, compliance and regulatory, beneficiaries and disputes)

Assess

- Whether the funds current approach meets member expectations and what existing strategies would allow the trustee to do so.

Manage

- Put a plan in place to manage the risk and it's consequences.

Communicate

- To members on the plan and implement.

Document

- Ensure trust deed is up to date, risk management plan is minuted and documented.

Poll

According to The ATO, over 70% of SMSF's have a corporate trustee?

True

False



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04

Positioning SMSF Advice

Positioning SMSF Risk Advice



De-risk the Trustee

This forms part of the trustee's broader risk management framework and avoid regulatory issues on acting in the best interests of members.



Protect against asset concentration

With reduced scale & unique investment decisions comes concentration of assets in particular asset classes that may make it difficult for the trustee to meet member & trust deed obligations.



Provide timely liquidity

Creating liquidity allows timely action, in line with trust deed, in the best interest of members and beneficiaries while also protecting longevity of the fund.

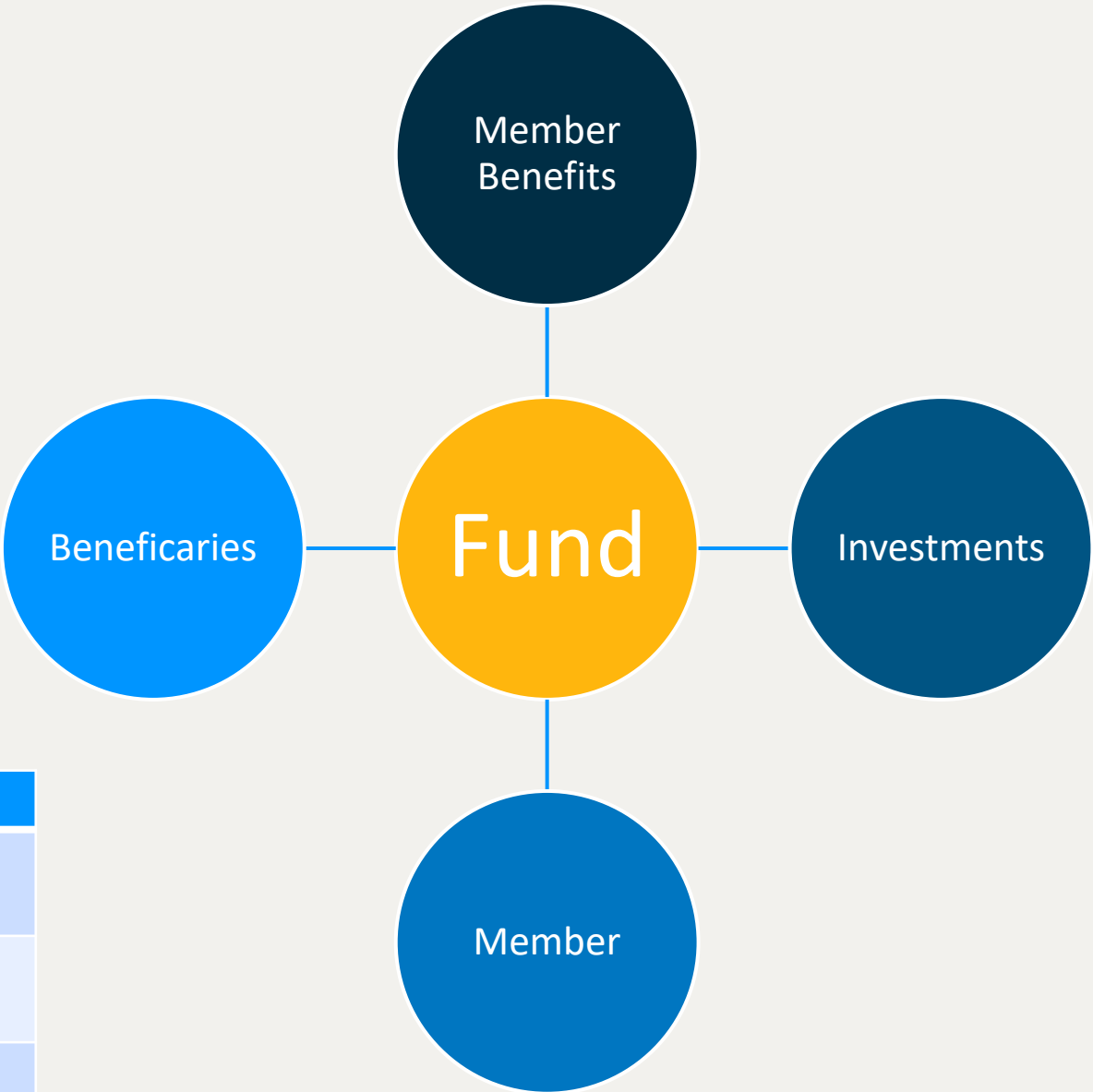
Problem Solving

How do we provide a solution to a problem, rather than a product?

Strategic Advice

- Start with a problem statement of what is facing the trustee & members
- Consider what strategies may allow the trustee to meet it's obligations and act in the best interest of members (not necessarily insurance – this is risk management advice!)
- Overlay cost of providing an insurance solution with the benefits for members, and in the context of both ease and accessibility of alternatives.

Strategy	Pros	Cons
Contributions	No current action required	Capital intensive, subject to caps and restrictions, may not be able to provide liquidity levels.
Sell Asset(s)	No current action required	Crystalise losses, time intensive, transaction costs, tax implications, opportunity costs
Insurance	Certainty, flexibility, Time-effective	Yearly cost (premium)





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05

Case Studies & Strategies

Case Study

Super Duper Super Fund

Risk Management

- Two member fund with equal balances and fund invested predominantly in a single property with a small amount of cash and equities.

Will consider 3 scenarios based on:

- Income stream
- Lump sum (inside super)
- Lump sum (outside super)

Super Duper Pty Ltd ATF Super Duper SMSF

Total Balance	\$1,200,000
---------------	-------------

Investments

Property	\$1,000,000
----------	-------------

Shares	\$100,000
--------	-----------

Cash	\$100,000
------	-----------

Member Balances

Member #1	\$350,000
-----------	-----------

Member #2	\$350,000
-----------	-----------

Debt (LRBA)

Property	(\$500,000)
----------	-------------

Insurance

Life & TPD per Member	\$500,000
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SMSF liquidity solutions

Scenario 1 – Death benefit pensions

-  Insurance owned and paid into the SMSF for Member 1
-  SMSF retains property and uses assets to fund death benefit pension
-  Can use insurance proceeds to reduce/remove outstanding LRBA debt
-  Must be able to meet ongoing upkeep costs of pension (cash earnings, rental earnings etc)
-  Recipient must be eligible to receive a pension (tax dependent)
-  Must consider transfer balance cap of recipient and ongoing viability of the fund (new members/single member fund/new trustee)

Key take-outs



- Allows for the maintenance of the property and the continuation of the fund
- Simplest solution
- Will it work for all beneficiaries? (ie is there a capital need?)
- What else should we consider?

Super Duper Pty Ltd ATF Super Duper SMSF Post Claim	
Total Balance	\$1,700,000
Investments	
Property	\$1,000,000
Shares	\$100,000
Cash	\$600,000
Member Balances	
Member #1	\$850,000
Member #2	\$350,000
Debt (LRBA)	
Property	(\$500,000)
Insurance	
Life & TPD Member 2	\$500,000



Super Duper Pty Ltd ATF Super Duper SMSF	
Total Balance	\$1,200,000
Investments	
Property	\$1,000,000
Shares	\$100,000
Cash	\$100,000
Member Balances	
Member #2	\$1,200,000 (\$350,000 accumulation + \$850,000 death benefit pension)
Debt (LRBA)	
Property	\$0

SMSF liquidity solutions

Scenario 2 – Lump sum Death benefit payment



Insurance owned and paid into the SMSF



SMSF receives life insurance benefit and forms part of the death benefit payable



May require an in-specie transfer of property as part of the death benefit for a spouse (including tax consequences for accumulation phase SMSF)



Adult children may have additional liquidity issues due to tax that the fund may not be able to pay, along with the in-specie transfer on the death benefit (see summary slide 35)

Key take-outs



- Simple solution
- May not actually solve liquidity issues
- Highly dependent on the Death benefit recipient dependency status
- Do we actually want to transfer the property as part of the benefit?
- Do we want the SMSF to continue?
- Can we create enough liquidity?

Super Duper Pty Ltd ATF Super Duper SMSF Post Claim	
Total Balance	\$1,700,000
Investments	
Property	\$1,000,000
Shares	\$100,000
Cash	\$600,000
Member Balances	
Member #1	\$1,100,000
Member #2	\$600,000
Debt (LRBA)	
Property	(\$500,000)
Insurance	
Life & TPD Member 2	\$500,000



Super Duper Pty Ltd ATF Super Duper SMSF	
Total Balance	\$600,000
Investments	
Property	\$400,000
Shares	\$100,000
Cash	\$100,000
Member Balances	
Member #2	\$600,000
Debt (LRBA)	
Property	\$0

SMSF liquidity solutions

Scenario 3 – Non-super lump sum

-  Insurance cross owned **outside** of superannuation
-  Contributed up to contribution caps to add liquidity
-  Does not form part of the death benefit amount
-  Can be used to reduce Limited Recourse Borrowing Arrangement (LRBA) and maintain property
-  No requirement to bring additional trustee or member of the fund
-  No requirement for in-specie transfer of property

Key take-outs



- Flexibility and choice created
- Commonly best for non-spouses
- Ability to maintain the property, SMSF and control
- Must consider taxation of benefit, such as TPD outside super to non-defined relatives
- Members may have different premiums due to health/age and equalisation may need to be considered
- How can we leverage this in insurance advice?

Super Duper Pty Ltd ATF Super Duper SMSF Post Claim	
Total Balance	\$1,200,000
Investments	
Property	\$1,000,000
Shares	\$100,000
Cash	\$100,000
Member Balances	
Member #1	\$350,000
Member #2	\$350,000
Debt (LRBA)	
Property	(\$500,000)
Member 2 contributes proceeds via NCC's, allowing liquidity to pay \$350k death benefit + clear \$250k of LRBA debt	
↓	
Super Duper Pty Ltd ATF Super Duper SMSF	
Total Balance	\$1,100,000
Investments	
Property	\$1,000,000
Shares	\$100,000
Cash	\$0
Member Balances	
Member #2	\$850,000
Debt (LRBA)	
Property	\$250,000

Liquidity Checklist

- ☐ Will liquidity be a problem in the event of a member's death or disability?
- ☐ Is there a need to retain the asset?
- ☐ Can benefit be paid out at all?
- ☐ Can benefit be paid out in-specie?
- ☐ Can benefit be paid out as a pension?
- ☐ If LRBA, can repayments still be funded?
- ☐ How much insurance is necessary?
- ☐ Will insurance proceeds pay off loan and/or boost fund balance and/or improve cash position?
- ☐ Can members make contributions to super (ie. Consider age, TSB, available cap space, etc)?
- ☐ What is impact on long term investment strategy of fund?



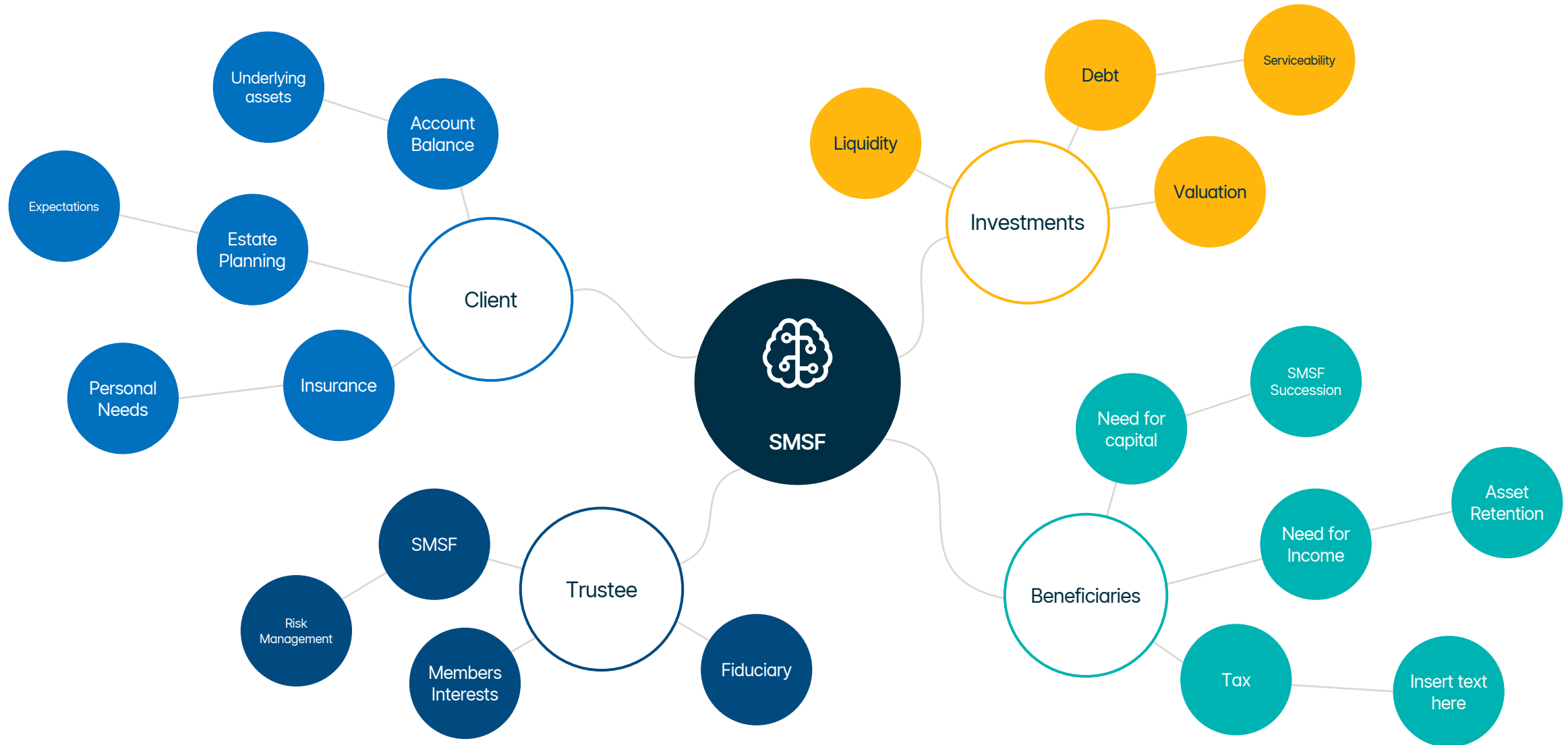
Summary

Structure Overview (Death Benefits)				
Relationship	Pension	In-Super Lump Sum	Outside Super Lump Sum	Considerations
Tax Dependant	✓	✓	✓	- The most options available but must consider beyond insurance the intentions for the fund, the needs for capital vs income, the maintenance of assets and tax considerations (depending on age) - Consider Transfer Balance Cap when utilising pensions
SIS Dependant (Non-Tax Dependant)	✗	✓	✓	Ability to maintain property, pay tax, need for income vs capital and future investments, future of the fund.
Non Tax or SIS Dependant	✗	✗	✓	- Contribution caps (consider reserving options as well) along. - Inability to fund from superannuation monies (considering sole purpose)

Tax Summary

Tax Overview		
Relationship	Pension	Lump Sum
Tax Dependant	• Tax-free if either deceased or recipient is over 60 • Under 60 – taxable component taxed at MTR with 15% tax offset	Life Cover – Tax Free TPD – 22% on taxable component (after proportioning via tax-free uplift)
SIS Dependant (Non-Tax Dependant)	N/A – Tax dependants only	Life Cover – 17% on taxed element + 32% on untaxed element
Non Tax or SIS Dependant	N/A (Outside Super Only)	• Life Cover – No CGT for original policy owner/acquired for no consideration • TPD – No CGT for ill/injured party or a first-degree relative (including trusts/beneficiaries of trusts) (Non Super)

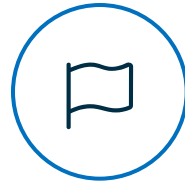
The Value of Mapping



Other SMSF Strategy Options

Retained external insurance & claims rollovers

External TPD benefits paid via an APRA fund, that is rolled across to an SMSF retaining status as a disability benefit.



Potential Benefits

- Crystallise tax-free uplift
- Retain benefits in concessional tax environment
- Open ability for income stream to better support long term needs and tax effectiveness.

s295-465 Tax deductibility of premiums

Ability for a trustee to claim a tax deduction for the cost of insurance premiums (does not mean that a trustee HAS to claim the deduction).



Tax efficiency

- Can experience the full value of the deduction (depending on the effective MTR of the SMSF/earnings)
- Will not always be passed to members in an APRA regulated fund.

s295-470 Future Liability deduction

Allows a trustee to elect to not claim a tax deduction for premiums in a particular year and instead can claim a deduction for the future liability to pay death or disability benefits.

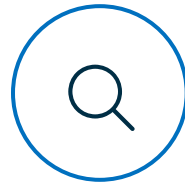


Future Tax Deduction

- Benefit amount x (Future service days/total service days)
- Benefits accumulation members as a tax offset
- E.g. \$1.5m benefit, at age 50 with a service date of 1991 would create a \$624k future liability tax deduction for the fund to exhaust over coming years.

Business Insurance

Using SMSF's to own and fund the provision of Buy/Sell arrangements?.



Sole Purpose

ATOID 2015/10 rules that this breaches the sole purpose test in relation to providing retirement benefits for members.



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06

Summary & Opportunity

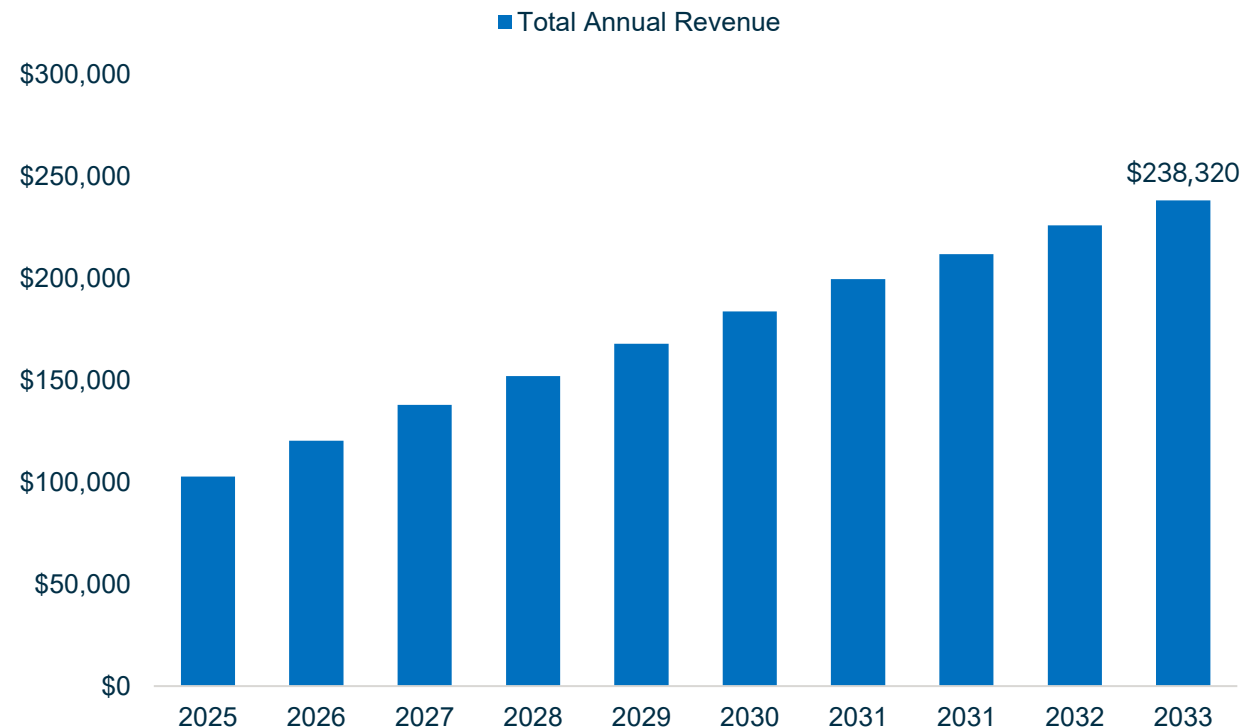
The Advice Opportunity

What is the value in engaging even a small portion of Property invested SMSF's?

The benefit

- Engage Trustees around strategic risk management advice in providing appropriate protection for members and fund assets – fee-based remuneration opportunity.
- Implementing individual insurance policies on behalf of individual members, with a commission-based remuneration model on this support, guidance & value.

The value of SMSF Insurance Advice – 10 SMSF Groups Per Year



Based on \$5k fee for new advice to SMSF Trustee + 2 members with \$4000 annual premium, accounting for 10% lapse rate over time

Summary & Next Steps

All new ethics hub with 5+ Ethics CPD Points



The Need

Is immense as Australians continue to look at SMSF's & property as a wealth building vehicle, without a full understanding of the broad responsibilities of the trustee

01

The Approach

Is based on de-risking the trustee, protecting members and providing a problem statement-based risk management engagement.

02

The Opportunity

Is considerable with the volume of SMSF's and the specialised nature of the advice, to add commercial value to advice businesses.

03

Further Education Sessions

Check out additional CPD accredited webinars and catch up
On prior webinars at the education hub



04

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Acenda 

The text "IS BECOMING" is in a small, white, uppercase, sans-serif font. Below it, the word "Acenda" is in a large, white, sans-serif font. To the right of "Acenda" is a stylized orange logo icon consisting of three overlapping leaf-like shapes.