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**FOREIGN INVESTORS**  
THE GOVERNMENT'S  
'CRACKDOWN'  
EXPLAINED

**SMSF LENDING**  
UNCERTAINTY  
ISN'T STOPPING  
INNOVATION

**PAPERLESS  
APPLICATIONS**  
NO LONGER WAITING  
ON TECHNOLOGY



**SMSF LENDING:  
BUSINESS AS  
NORMAL ... BUT  
FOR HOW LONG**



With repercussions from the Financial System Inquiry in full swing, the superannuation sector is waiting to find out whether SMSF lending will remain in the game. **Maya Breen** spoke to five leading lenders to hear their thoughts on where SMSFs are heading and whether there is still room for innovation in self-managed super products

**ALTHOUGH SMSFs** are still one of the fastest-growing slices of the superannuation sector, the future of SMSF lending is in question as a result of the Financial System Inquiry (FSI) Recommendation 8, calling for a stop to direct borrowing by SMSFs using limited recourse borrowing arrangements (LRBA).

The government will by now be considering the feedback submitted by industry players, but what will be the implications if the FSI recommendation goes ahead? Is it likely and should brokers be concerned and preparing for potential changes?

“I do not believe the FSI’s recommendation should be cause for concern,” says Suresh Pillai, general manager of non-bank lender Liberty Financial. “It is important to remember that the government is still consulting with stakeholders about the FSI’s recommendations, and it is possible that we will end up with an optimal and balanced outcome where SMSFs are still able to borrow but with additional conditions in place. Let’s also not forget that if the recommendation is implemented in its current form, it could deprive Australians of a viable investment choice and may just end up moving gearing into more risky investment areas.”

## THE PANELLISTS



**Martine Jager**,  
CEO, RAMS, and general manager,  
mortgage broking, St. George  
Banking Group



**Suresh Pillai**,  
general manager, Liberty



**Per Amundsen**,  
director, Thinktank



**Sinclair Taylor**,  
head of self-managed  
superannuation funds, Westpac



**Cory Bannister**,  
vice president and head  
of distribution, La Trobe

## A SNAPSHOT OF THE SMSF SECTOR

In Dec 2014



545,334

self-managed super funds



1,034,497

members

In 2012–13, % of SMSF funds run by



1: 22.6%



2: 69.5%

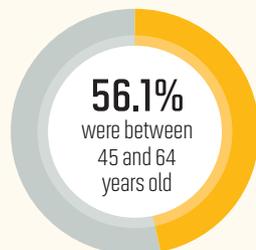


3: 3.9%



4: 4.1%

Age of SMSF members in June 2014



Source: ATO SMSF Quarterly Report, Dec 2014

Per Amundsen, director of specialist lender Thinktank, also doesn't believe there will be a complete ban, but more likely only adjustments to specific issues. "I think all of us involved in the sector have to be very aware that there may be changes that we will have to adjust to, but the consensus seems to be that a return to a total prohibition will not result from the FSI recommendation," Amundsen says.

will be a sudden influx of people rushing to get an SMSF loan in case they go, but we haven't seen that."

### Why does the FSI want to stop direct borrowing by SMSFs?

The MFAA will submit a joint submission to government in defence of SMSF borrowing, and on how it will impact on its members if

## "St.George will continue to work with the broker community to help them get the best out of our current SMSF product"

Martine Jäger, CEO, RAMS, and general manager, mortgage broking, St.George Banking Group

Some lenders see an upside to the current controversy, with La Trobe vice president and head of distribution Cory Bannister pointing out: "In the short term, it is business as usual; in fact, the uncertainty around the product's future has encouraged more activity in this space, so opportunities for brokers have currently increased."

But the non-bank does warn brokers who specialise solely in SMSF loans to start looking to diversify, as a precaution. "We believe all brokerage businesses should ensure they have a diverse product offering, not relying too heavily on any one borrower or asset class – this is something we advocate when speaking with our clients; simply don't put all of your eggs in one basket," Bannister says.

"We would be surprised if SMSF lending is prohibited entirely as we genuinely feel it is a positive mechanism for consumers to accumulate wealth for their retirement; however, we expect limitations to be placed on the product's terms, which if appropriate will ensure the expansion into SMSF will continue to pay dividends for brokers for some time."

Westpac is waiting for the decision from the government, but Sinclair Taylor, head of self-managed superannuation funds, says it is still legal today to make a loan to an SMSF. "It's definitely a wait-and-see environment. We haven't seen a significant increase; there's certainly been some speculation that there

the recommendation goes ahead, but what are the reasons behind the FSI's concerns?

According to the *FSI Final Report*, the two objectives supporting its recommendation were to prevent the accumulation of risk in the super system and financial system, and to steer the use of superannuation back towards a "savings vehicle for retirement income, rather than a broader wealth management vehicle".

However, whether these reasons will bring the recommendation to fruition is another matter. Like the MFAA, the SMSF Professionals' Association of Australia (SPAA) doesn't agree with the report, announcing that they do not support the recommendation as "there is little evidence that borrowing in superannuation is causing a build of excessive risk or systemic risk in superannuation".

The SPAA believes that, to reduce any risk from borrowing in superannuation, other alternative solutions such as licensing advice on LRBA and limiting the role of personal guarantees in LRBA could be implemented.

Some lenders, like St.George and AMP, which are heavily involved in the superannuation space, have preferred to wait for the outcome from the government before commenting on how the superannuation sector may change, but others don't agree with Recommendation 8 for a number of reasons.

Thinktank's Amundsen says the objectives "relate mainly to a possible system risk in the

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## “We believe it is more likely that there will be some particular adjustments that address specific issues, rather than a complete ban”

Per Amundsen, director, Thinktank

### FINANCIAL SYSTEM INQUIRY (FSI) RECOMMENDATION 8

 Direct borrowing by superannuation funds: “Remove the exception to the general prohibition on direct borrowing for limited recourse borrowing arrangements by superannuation funds”

Source: FSI Final Report, p86

 In 24 September 2007, superannuation laws were amended to allow an SMSF to purchase an investment asset through a limited recourse borrowing arrangement

Source: ATO

### WESTPAC SMSF SURVEY: HOW DIFFICULT IS SMSF?

Out of 1,000 SMSF trustees:

**58%** of respondents said it was as demanding as they thought it was going to be

**30%** of respondents said it was harder than they had anticipated

event of a major downturn in property markets, and an impression that gearing was being used more as a tool of speculative investment rather than for long-term retirement savings as SMSFs were intended.

“We don’t wholly agree with those impressions and so don’t come to the same conclusion as the inquiry. There are certainly some things that could be improved, and we think it would be more productive to focus on what those are and then address them individually rather than take the very broad approach that has been recommended.”

Pillai of Liberty says that perspective has its benefits. “I can see how people have concerns about geared property investment in light of some of the recent growth in property prices. So of course, if you are pessimistic about property you will have concerns about the build-up of risk due to geared property investment by SMSFs. However, if you have a longer-term perspective, an investment in a quality residential or commercial property could yield both a healthy rental stream and capital appreciation.”

La Trobe’s Bannister points out it’s not the borrowing by SMSFs that is the issue but the strategy. “Borrowing via SMSFs is not a bad thing, if it is coupled with an appropriate ‘managed’ investment strategy. The problem lies when borrowers are ill-advised or do not have an appropriate strategy to manage their SMSF investment.”

Westpac believes it is important to remember that most Australians are not interested in SMSF. “We are of the view that SMSF is not right for most Australians,” says Taylor. “We currently have, if you look at the market data, 8% of Australians who have super have an SMSF – hence 92% of Australians don’t have one. So a small number of people who really know what they’re doing should be in this space, and we want to help

those individuals make good decisions but acknowledging of course that they themselves have to make those decisions, and that is the challenge of running your own super fund: you are in the driver’s seat.”

However, Thinktank finds that the report has misinterpreted the facts on both of its objective points, “starting with an overestimation of how significant direct property – and that which is geared – will become as a percentage of total SMSF assets,” says Amundsen. “The assumptions by the FSI are well beyond what seems to be reasonable, and so is the suggestion that geared direct property cannot be a savings vehicle for retirement.”

## “I do not believe that the FSI’s recommendation should be cause for concern”

Suresh Pillai,  
general manager, Liberty

### Waiting game

On whether there is still room for innovation in SMSF products in light of a potential regulatory change, there are mixed responses from our lender panel.

Despite the uncertain climate, St. George says it will continue to move SMSF products forward. “As well as innovation, there will also be a focus on education,” says mortgage broking general manager Martine Jager. “It is a big commitment for someone to head down the road of an SMSF, and given the trend appears to be that an increasing number of people are choosing this option, we believe education will be crucial.”

But Liberty says that in the current climate it’s more about improvement than innovation. “I think SMSF lending products are at an inflexion point where prudent and sensible refinements can cement SMSF loans as a valuable and responsible proposition for brokers and borrowers,” Pillai explains. “These

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## NOT ALL SMSFs ARE AFTER RESIDENTIAL INVESTMENT

"There's certainly a perception, and this is often media-led, that every SMSF is rushing out and buying residential property, which is just simply not true," says Sinclair Taylor of Westpac.

Taylor says the level of assets inside SMSFs devoted to residential property is \$21bn. "That is only 4% of all of the assets inside self-managed super, so 4% of the pie; and it has been 4% for several years now."

A very small number of SMSFs are using a property-gearing strategy. ATO statistics show that, at the end of the June 2013 financial year, only 2.7% of all SMSFs had a loan in place.

"The market commentary would suggest that everyone setting up an SMSF is doing so almost for the sole purpose of buying a residential property; it just simply isn't the case," Taylor says.

SMSF is still Australia's largest and fastest-growing superannuation segment, but not all trustees are including property gearing, which is what the FSI is addressing.



refinements could include things such as a more holistic servicing approach and consistent approaches across the industry to professional advice requirements."

Thinktank also believes the focus for the future lies more in the realm of professional advice than innovation. "It is perhaps less of a question of innovation than one of having a very good understanding of what can and cannot be done within the regulations," says Amundsen. "When borrowers have good professional advice this is a big help, but you also have to be very aware yourselves of what those regulations are. Knowing when you can do something that may be out of the ordinary but still within those regulations can be very helpful in allowing you to work effectively with the borrower's professional team."

La Trobe's Bannister says: "As a lender known for innovation, we would like to think there are always opportunities to improve products. However, innovation in the SMSF lending space is likely to have been placed on hold until the government responds to the FSI recommendations, which have the potential to directly impact on the availability and terms of this product."

Westpac has recently removed its requirement for borrowers to present a financial advice certificate. "What we've done is replace it with a trustee acknowledgement,

**"There is a degree of uncertainty as to whether gearing will continue and how the government may respond to that recommendation, but the sector is well managed"** Sinclair Taylor,

head of self-managed superannuation funds, Westpac

absolutely recommend that people get it."

So for the time being, until the SMSF sector hears what conclusion the government has reached, SMSF lending is a little in limbo as to where it will end up. But one thing is for sure, the FSI report has created a strong debate within the industry on SMSFs.

Thinktank's Amundsen concludes: "We are very hopeful of a well-informed and unemotional debate on the subject that results in any changes being for the good and

**"In the short term, it is business as usual; in fact, the uncertainty around the product's future has encouraged more activity in this space, so opportunities for brokers have currently increased"** Cory Bannister, vice president and

head of distribution, La Trobe

where the trustees themselves are making comment or an undertaking to the bank that they've thought about all the issues that a planner would typically talk to them about and before they enter into the transaction," Taylor says. "But we're not diminishing the importance of financial advice; we still

addressing specific issues rather than a knee-jerk reaction. Our particular involvement in the SME sector leaves us believing that SMSF LRBAs are an excellent vehicle for building retirement savings and actually encourage SME owner-operators to focus on providing for their financial needs in retirement." **MFA**